

**AN ANALYSIS OF ALTERNATIVE
"SWAP" PROPOSALS AND THEIR
POTENTIAL IMPLICATIONS
FOR STATES**

FINAL REPORT

October 1995

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This research was funded by the Health Care Financing Administration (HCFA), Contract 500-92-0024 DO#6. Opinions expressed are those of the authors and do not necessarily reflect the positions of HCFA or The Urban Institute. The authors are grateful for comments from John Holahan and Brigid Goody.

I. Introduction

“Swap” proposals are legislative approaches designed to more clearly divide the program responsibilities of the federal government from state governments. These proposals tend to focus on areas such as health care and social welfare, where either jointly financed programs exist or separate programs with similar objectives are being run by the different levels of government. Swap proposals are sometimes also proposed by those who want to reduce the size of the federal government.

This paper explores the swap proposals that are currently being considered in Congress as well as alternatives that have been proposed in the past or which are modifications to those being considered. We then review the theoretical bases for dividing particular responsibilities across different levels of government. We also synthesize the available evidence on the likely behavioral responses of states following such a re-ordering of responsibilities. Finally, we demonstrate empirically some possible scenarios of the impact of alternative swap proposals across states.

There is an intuitive appeal to dividing government responsibilities. Forcing complex coordination between multiple bureaucracies can be confusing and inefficient. Also, with no single entity being primarily responsible for a particular program, there is no clear source responsible for the failures or shortcomings of the program. And with regard to programs that are jointly financed, the financial impact of program inefficiencies are blunted for both parties, with each only bearing a portion of the costs incurred. This also creates incentives for states to attempt to “game” the program, leading to inefficiencies that arise specifically because of joint

financing.¹

A number of swap-type proposals have been introduced. In conjunction with consolidation of many categorical grants into many fewer "block grants" to states, Ronald Reagan's fiscal 1983 budget proposal included a swap plan. Under the Reagan swap, the federal government would have taken complete responsibility for the Medicaid program while the states would have taken-over Aid to Families with Dependent Children (AFDC) and the Food Stamp Program.² While the swap component of Reagan's budget proposal did not pass, recent proposals are reminiscent of that framework.

Interest in swap proposals was revived by Senator Nancy Kassebaum as a means for streamlining government activities and not for deficit reduction purposes. The Welfare and Medicaid Responsibility Exchange Act of 1995 (S. 140) was introduced by Senator Kassebaum on January 4 of 1995. Later that same month, the Senator released materials indicating that she would soon introduce a revised version of that bill. That bill was introduced on April 6, 1995 as S. 707. The policies of the original bill and the policies of the revised version are described below.

The Welfare and Medicaid Responsibility Exchange Act, originally introduced as S. 1891 in 1994, provides for a clear division of financing responsibilities between the federal and state governments for a number of public aid related programs. As of October 1, 2001, the states

¹For example, there are a number of documented situations where state governments have manipulated the Medicaid program to help fund other state functions. See Leighton Ku and Teresa Coughlin, "Medicaid Disproportionate Share and Other Special Financing Programs: A Fiscal Dilemma for States and the Federal Government," Urban Institute Report, December 1994.

²Executive Office of the President, Office of Management and Budget, *Major Themes and Additional Budget Details: Fiscal Year 1983*, U.S. Government Printing Office, Washington, DC.

would be relieved of any financial responsibility for the Medicaid program, while the federal government would be relieved of any financing responsibilities for Aid to Families with Dependent Children (AFDC), Food Stamps, the Special Supplemental Food Program for Women Infants and Children (WIC), and JOBS.

During a transition period (fiscal years 1997 through 2001) the states and the federal government would be held harmless with respect to AFDC, Food Stamps and WIC. The federal government would make payments to the state governments during this period equal to the federal share of spending on these programs from July 1, 1995 through June 30, 1996, inflated by increases in the consumer price index for urban areas (CPI-U) since that year, and adjusted to take into account increases in the number of program recipients in the state. States, for their part, would be required to "maintain effort" with respect to these three programs for fiscal years 1997-2001, i.e., total spending (federal plus state dollars) must be kept at or above the total base amount, inflated annually for prices and recipient growth. States must also continue to pay their share of the Medicaid program during this phase-in period. There is no federal payment to be made to states in lieu of funding for the JOBS program, and no state maintenance of effort required.

As of October 1, 2001, federal payments to states for AFDC, Food Stamps and WIC cease and the requirement that states maintain effort ends as well. At that time state payments toward Medicaid would stop, and that program would become fully federalized. Upon federalization, there is substantial leeway for the federal government to restructure the Medicaid program.

The Welfare and Medicaid Responsibility Exchange Act of 1995

States During Transition Period		Following Transition Period	
<i>Federal Dollars Flowing In To States:</i>	<i>State Dollars Flowing Out:</i>	<i>State Dollars Only For:</i>	<i>Federal Dollars On Newly Federalized Programs:</i>
Federal Share of AFDC	Total AFDC	Total AFDC (level at state's discretion)	Total Medicaid (may take new form)
Federal Share of WIC	Total WIC	Total WIC (level at state's discretion)	
Federal Share of Food Stamps	Total Food Stamps	Total Food Stamps (level at state's discretion)	
	Total JOBS (not required)	Total JOBS (level at state's discretion)	
	State Share of Medicaid		

The second version of the "swap" proposal would ultimately divide responsibility for the Medicaid program between the federal government and the states, instead of giving the federal government the full obligation. The federal government would assume the portion of the Medicaid program associated with the elderly and the disabled, while the states would be left with the Medicaid benefits for the AFDC and other low income populations.

The Revised Welfare and Medicaid Responsibility Exchange Act of 1995

States During Transition Period		Following Transition Period	
<i>Federal Dollars Flowing In To States:</i>	<i>State Dollars Flowing Out:</i>	<i>Federal Payments Stop. State Dollars Flowing Out:</i>	<i>Federal Dollars On Newly Federalized Programs:</i>
Federal Share of AFDC	Total AFDC	Total AFDC (not required)	Total Medicaid for Elderly and Disabled, and all Long Term Care (may take new form)
Federal Share of WIC	Total WIC	Total WIC (not required)	
Federal Share of Food Stamps	Total Food Stamps	Total Food Stamps (not required)	
	Total JOBS (not required)	Total JOBS (not required)	
	State Share of Medicaid	Total Medicaid for AFDC & Low Income (not required)	

The change was the result of preliminary Congressional Budget Office and Congressional Research Service analyses which estimated that the original proposal would lead to an increase in the federal responsibility of more than \$20 billion in the first fully phased-in year.

A third proposal which roughly falls within the category of "swap" proposals was outlined by Alice Rivlin.³ While not a formal legislative proposal, Rivlin outlines a federalism framework for what she calls "dividing the job". Her policy agenda includes the following five components:

- The federal government leads reform of the health care financing system, focusing on

³ Alice Rivlin, *Reviving the American Dream: The Economy, the States and the Federal Government*, The Brookings Institution, Washington, DC, 1992.

universal coverage and cost containment.

- The states take responsibility for implementing a “productivity agenda” for revitalizing economies and increasing incomes. Such an agenda includes: education and skills training, child care, housing, infrastructure, and economic development.
- The following programs devolve to the states, or are eliminated over time: elementary and secondary education, job training, economic and community development, housing, most highways and other transportation, social services, and some pollution control programs. A few functions would remain federal and perhaps be enhanced, including higher education scholarships for low-income students, federal support for scientific research, and air traffic control.
- The federal government brings its budget into surplus, including social security, through: devolving the mentioned domestic programs to the states, imposing health insurance taxes and transferring Medicaid spending to a health insurance trust fund, and reducing other federal spending.
- States strengthen their tax systems and increase revenue by implementing one or more common taxes (same base, same rate), and sharing the proceeds.

A number of important functions would remain the joint responsibility of the federal government and the states, including environmental protection and welfare for families with children. With respect to AFDC, Rivlin expects both states and the federal government to maintain an interest in reducing welfare dependency. Her expectation is that states would improve education, training, and child care for recipients, while the federal government would make tax system changes such that the after-tax return for low wage work would be improved. The Clinton Administration’s expansion of the earned income tax credit (EITC) could be thought of as a first step in addressing the latter.

The remainder of this paper is divided into four sections. Section II provides a theoretical discussion of the criteria that might be used for dividing public responsibilities across different levels of government. A brief summary is presented at the beginning of the section. Section III

reviews the empirical economic literature for insight into the ways in which changes in the structure of intergovernmental grants are likely to affect state spending. Section IV presents our simulations of the effects of alternative swaps on spending across states. Section V presents our conclusions.

II. Criteria for Dividing Responsibilities Across Levels of Government

There are an infinite number of ways in which programs can be divided between federal and state jurisdictions. Choosing criteria for dividing responsibilities can be difficult. In addition to determining the proper theoretical roles of each level of government, budget concerns can be significant as well. Most proposals are intended to be relatively budget neutral, particularly in the short run. As a result, criteria are often relaxed in order to achieve the appropriate budget mix. Nonetheless, budget neutrality can be difficult to achieve in anything but the aggregate from the perspective of the states because of variations in program spending across states. This is particularly the case when dealing with Medicaid and AFDC.

In general, the economic literature supports placing responsibility for programs at a decentralized (e.g., state) level. Important exceptions to this rule exist, however, and they can be identified according to three main criteria⁴:

- Whether or not a program, when left to the states, would generate spillover effects for other states or localities (perhaps the most often cited criteria).
- Whether or not economies of scale can be found by federalizing a particular program.
- The extent to which states vary in their demand for a public good or service.

⁴Wallace E. Oates, *Fiscal Federalism*, New York, Harcourt Brace Jovanovich, 1972.

Programs implemented at the state or local level may generate externalities, or spillover effects, for other states and/or localities. In other words, one state's program may have the potential to affect the welfare of residents in another state, either positively or negatively. Since each state or locality is not likely to take into account the potential effects of each program on their neighbors when they are designing them, it is, in general, socially efficient for such policies to be implemented at a more centralized level. If such policies are not centralized with the broader national interest taken into account, individual states or localities will be likely to either underprovide or overprovide such services from the perspective of society as a whole. Programs generating spillover effects are also referred to as being of shared national purpose.

Benefit spillovers are, however, likely to be the most difficult criteria to measure. For example, how would one quantify the value that persons in one state place on the fact that medical care for low income populations or education are provided in another state? Some might also include the value of having services available in other communities in the event that they might move there at some date in the future.

Redistribution of income is one important example of public policies with strong spillover effects. There are a number of ways in which spillover effects enter into decisions about the governmental locus of redistribution of income. First is that there is a widely perceived national interest in the poor outside of taxpayers' own jurisdictions.⁵ Individuals' concerns about low

⁵Advisory Commission on Intergovernmental Relations, "An Agenda for American Federalism: Restoring Confidence and Competence," one volume in a Commission Report, *The Federal Role in the Federal System: The Dynamics of Growth*, US Government Printing Office, Washington, DC, 1981. Also, Helen F. Ladd and Fred C. Doolittle, "Which Level of Government Should Assist the Poor?" *National Tax Journal*, vol. 35, September, 1982. Ladd and Doolittle also address Mark Pauly's formal proof [in "Income Redistribution as a Local Public Good," *Journal of Public Economics*, vol. 2, no. 1, February, 1973] that redistributive programs should be decentralized. The authors note that the conditions that Pauly requires in his proof, that non-poor residents are concerned only about poor people in their own jurisdiction, and that welfare participants do not move in search of higher benefits, are both disproved by

income populations tend to extend to those living all across the U.S. Second, the relative ease of geographic mobility in the United States makes decentralization of redistributive policies extremely difficult to implement.⁶ If a state or local government were to impose a progressive income tax, the revenue for which would be distributed according to need, there would probably be an exodus of its high income people. As a result, states might begin to compete in reducing the levels of their income maintenance benefits, leading to benefit levels which are lower than what any state would consider desirable. The possibility of this dynamic is reflected in the relative lack of progressive state and local income tax systems in the United States.

In addition, from an equity perspective, it is best to redistribute income at the highest level of government, so that the burden of assisting the needy is spread over as many higher income units as possible. The federal income tax treats families with the same income levels approximately the same, regardless of state of residence.

The second criterion is whether there are economies of scale in the production of the services in question over multiple communities. In other words, if the service were to be

available evidence.

⁶Wallace E. Oates, "An Economist's Perspective on Fiscal Federalism," in *The Political Economy of Fiscal Federalism*, Wallace E. Oates, ed., D.C. Heath and Company, Lexington, MA, 1977. This hypothesis is supported by empirical work by Lawrence Southwick, Jr., "Public Welfare Programs and Recipient Migration," *Growth and Change*, vol. 12, no. 4, October, 1981; Rebecca Blank, "The Effect of Welfare and Wage Levels on the Location Decisions of Female-Headed Households," *Journal of Urban Economics*, vol. 24, 1988. Relatedly, Rebecca L. Clark, "Does Welfare Affect Migration?" Population Studies Center, The Urban Institute, May 1990, finds that high welfare payments inhibit out-migration of welfare recipients and potential recipients. The migration theory is, however, disputed by Mark Shroder, "Games the States Don't Play: Welfare Benefits and the Theory of Fiscal Federalism," *The Review of Economics and Statistics*, vol. 77, no. 1, 1995.

In "On the Decentralized Provision of Public Goods with Spillovers in the Presence of Household Mobility," *Regional Science and Urban Economics*, vol. 23, 1993, Dietmar Wellisch disputes the work done by Oates. His theoretical model, however, appears to be dependent upon the homogeneity of populations. In addition, his argument is one of efficiency alone, and that limited perspective is not appropriate in studying redistributive programs which are equity, as opposed to efficiency, oriented.

produced at a more inclusive level, would the per unit cost of production be lower? It would be socially inefficient to implement programs in a decentralized manner that could be run at lower cost at higher levels of government. One example is the administrative savings from the central government collecting income taxes.

The third criterion is the extent to which there is a consensus regarding the appropriate level of spending on a particular public service or program. If states vary considerably in their willingness to invest in particular goods, the strength of those preferences might reasonably be taken into account.⁷ Powerful differences in attitudes and preferences may be allowed to override concerns with economies of scale, for example. On the other hand, if a state has a strong preference for low levels of a service that generates large spillover effects, those preferences might appropriately be overridden. For an extreme example, let us assume that a given state, left to itself, would spend no public dollars on national defense. Any spending on national defense by other states will, however, benefit that state as a consequence of its geographic proximity. Permitting that state and its residents to “opt-out” of national defense spending allows them to accrue the benefits resulting from others’ investments at no cost to themselves. This is obviously inequitable, but is also likely to lead to inefficiently low investment in national defense, as other states attempt to be “free riders” as well.

Rivlin’s division of public service burdens is roughly consistent with the theoretical divisions outlined above. Rivlin relegates services related to increasing productivity⁸ to state/local

⁷Edward M. Gramlich, “The Economics of Fiscal Federalism and Its Reform,” in *The Changing Face of Fiscal Federalism*, Thomas R. Swartz and John E. Peck, eds., ME Sharpe, Inc., Armonk, New York, 1990.

⁸This role would include education and skills training, child care, housing, infrastructure, and economic development. Rivlin envisions competition among states to improve services and attract businesses.

governments, while the federal government would be required to develop and control those services which serve broad redistributive functions and which have substantial spillover effects (e.g., scientific research, higher education scholarships). Interestingly, however, she maintains one prominent redistributive program, AFDC, as a shared program. In this case she sees the program divided in its objectives between redistribution of income (a clearly central government role) and education/training and job placement (a more productivity oriented, and thus decentralized, role).

In contrast, the swap proposals being considered by members of Congress do not tend to conform to the conceptual frameworks detailed here, nor do they seem to have been developed with a theoretical framework in mind. The Kassebaum proposal partitions a number of significant redistributive programs (AFDC, Food Stamps, WIC) to the states, while Medicaid (another redistributive program) is divided up between federal and state governments. All of these programs have significant spillover effects. The elimination of the JOBS training program from the federal government's agenda is, however, consistent with the general framework outlined previously.

III. How Are Changes in the Structure of Intergovernmental Grants Likely to Affect State Spending?

Predicting how changes in current intergovernmental grants are likely to affect state's own spending on particular programs is a very uncertain task. Although there has been considerable theoretical and some empirical work on the ways in which imposing different types of grants may affect state decisions on spending, there has been very little work done on the termination of grant

programs and the impacts of doing so. Analysts making such predictions are left to what amounts to guesswork based upon working backwards from the existing theory. Although such analysis may give us some guidance as to what to expect “post swap”, the varying preferences of different jurisdictions and local financial pressures mounting over time are likely to be more influential over state behavioral changes than any economic incentives that we might be able to predict a priori.

The federal contribution to the AFDC and Medicaid programs is in the form of an open-ended matching grant. As such, the federal assistance acts to lower the price to states of providing these “goods”. The response that this price reduction engenders from each state will be a function of the state government’s price elasticity of demand for the good. As Break⁹ explains, a grant is fiscally neutral if the state spends the same amount of its own funds on the program as it would have if there had been no grant (a price elasticity equal to 1). In this case, total spending on the program (state plus federal) will have increased as a result of the grant by the amount of the federal grant. If however, the price elasticity of demand for the program is less than 1, then the state will spend less than it would have without the grant, and the change in total spending could be higher, lower, or the same depending upon the magnitude of the price response. And in the third case, if the price elasticity exceeds unity, the state will spend more of its own funds in the presence of the grant than it would have otherwise.

One goal of federal matching grants is generally perceived to be to encourage additional spending by states on the particular program. This is a goal that is called into question by a significant number of people with regard to the Medicaid and AFDC programs. Regardless, in cases where states exhibit low price elasticities of demand for a given program, matching grants

⁹George F. Break, *Financing Government in a Federal System*, Brookings Institution, Washington, DC, 1980.

are not the optimal form of intergovernmental aid -- the aid would tend to be diverted to other state uses.

An additional complication is that price elasticities for a specific program are likely to differ across states, as preferences and tastes often vary across geographic locations. As a result, we can expect the magnitude of behavioral effects resulting from a change in the structure of a grant program to have different effects in different states.

With the termination of a matching grant program, as would be the case for both AFDC and at least portions of the Medicaid program under the swaps being considered in Congress, the result is to effectively increase the price of services to the state. The state returns to the situation where it faces 100 percent of the costs of providing the service to its residents. To the extent that there are positive externalities to a state's consumption of the service, such a price change is likely to decrease the state's purchase of the program's services to levels that are socially inefficient.¹⁰ The state will decide upon a level of spending that does not take into account the positive effects of the service for other states.

In his empirical work, Orr¹¹ estimated both price effects and income effects generated by the AFDC program.¹² He found that no significant income effect was stimulated by the AFDC program; the only significant effect on states' choice of benefit levels was a price effect, the result

¹⁰ An example of a positive externality with respect to AFDC/Medicaid spending is the case where individuals living in one state place a value on medical or income assistance being provided to low income individuals in other states.

¹¹ Larry L. Orr, "Income Transfers as a Public Good: An Application to AFDC," *American Economic Review*, vol. 66, June, 1976.

¹² While price elasticities measure the state's change in demand as a result of an effective change in price, income elasticities measure the state's change in demand as a result of federal dollars flowing into the state, an effective increase in the state government's income.

of the lower marginal price afforded by the federal matching rate. This is not surprising since the absolute dollars contributed to the AFDC program per taxpayer in the state is very small relative to per capita income. His estimated elasticity with respect to marginal price was -.23. Orr notes however, that due to a potential econometric problem, the coefficient on the price effect might be biased; the price effect of the matching rate might actually be stronger than indicated in the equation. He also estimated the effect of converting the AFDC matching grant into a federally funded benefit floor. Under this construction, states would be given an equivalent amount of federal money as they were under the matching formula, but no state match would be required -- states could supplement the federal dollars if they wished. In this case Orr found that benefit levels would, on average, have fallen by approximately 16 percent annually in the 1968 to 1972 time period.

As Gramlich and Laren¹³ noted, when turning responsibility for AFDC back to the states, the relative price increase is greatest for low income states. Consequently, the decrease in program spending can be expected to be greatest in those states. For example, the matching rate for Connecticut, a state with 11.8 percent of its population under 150 percent of poverty, was 50 percent in fiscal year 1993. It cost Connecticut only 50 cents for each dollar of AFDC benefits. Following the "turn back" of AFDC, Connecticut would experience a price increase of about 67 percent.¹⁴ By contrast, the state of Mississippi, with 39 percent of its population below 150 percent of poverty, had a fiscal year 1993 matching rate of 79 percent. Post swap, the price of

¹³Edward M. Gramlich and Deborah S. Laren, "The New Federalism," in *Setting National Priorities: The 1983 Budget*, Joseph A. Pechman, ed., The Brookings Institution, Washington, DC, 1982.

¹⁴Measuring the price increase against the average of initial and final prices, as Gramlich and Laren suggest.

Mississippi's AFDC benefits will have risen by approximately 130 percent.

Any income effect that might occur in response to shifting full responsibility for AFDC to the states would be negative. The discontinuation of federal AFDC dollars is equivalent to a decrease in state government income and should prompt a decrease in demand if any demand change were experienced as a result. Those states currently receiving high levels of federal AFDC dollars relative to the size of the state's budget should experience the most significant relative decreases in demand for the AFDC program. Thus both the price and income effects of terminating the federal funding of a program like AFDC would work to reduce state efforts in this area.

In other work, Gramlich¹⁵ estimated the effects of a number of the proposals included in the Reagan swap plan, including devolution of AFDC and Food Stamps to the states.¹⁶ His estimates imply that states would respond to the increase in the marginal cost of AFDC benefits by lowering benefits an average of 56.4 percent and would lower them even further to the extent that states respond to the responses of other states -- a total of 97.5 percent. He also found that devolving food stamps to the states would exert significant downward pressure on the level of total cash and non-cash benefits.

On the other hand, the lifting of a portion of the Medicaid burden, as the federal government assumes full responsibility for certain components of the program, should affect state governments in much the same way that a lump-sum intergovernmental income transfer would

¹⁵Edward M. Gramlich, "An Econometric Examination of the New Federalism," *Brookings Papers on Economic Activity*, no. 2, 1982.

¹⁶Although the original Reagan proposal would have turned Food Stamps back to the states, the proposal was later changed in response to pressures from governors, and retained at the federal level.

affect the state. Grants to state/local governments tend to increase public spending to a greater extent than does an equivalent increase in private income. In other words, dollars tend to stick where they hit -- a fiscal theory known popularly as the "flypaper effect".¹⁷ Break¹⁸ notes that a \$1 increase in private income tends to translate into a 5¢ to 10¢ increase in state and local government public spending, whereas a \$1 increase in state and local government income will tend to increase public spending in the range of 25¢ to \$1. The portion of the income increase not going to increased government spending is consumed by the private sector, either through direct private spending, saving, or investment, or indirectly through decreases in existing tax burdens. The decreased state and local burden for a portion of the Medicaid program can therefore be expected to be converted to other public spending (either on those programs newly made the responsibility of states, or on other state priorities) on the order of 25 to 100 percent of the savings, while the remaining 0 to 75 percent of the public income may be used to allay private tax burdens.

While the predicted ranges of these effects are large, the hardest state/local government effects to predict are those for food stamps, WIC, and JOBS programs. Since these are virtually fully federally financed programs, we have no evidence as to the propensity that states have to spend their own funds on these programs. And since there are no maintenance of effort requirements on the states that they continue any spending on these programs following a transition period, the only lower bound that we can place on estimates of the behavioral effects is

¹⁷See Paul Courant, Edward Gränlich, Daniel Rubinfeld, "The Stimulative Effects of Intergovernmental Grants: Or Why Money Sticks Where It Hits," in *Fiscal Federalism and Grants-in-Aid*, Peter Mieszkowski and William Oakland, eds., Urban Institute Press, Washington, D.C. 1979, for a theoretical exposition for why the flypaper effect occurs.

¹⁸op. cit.

that the state/local governments totally eliminate them. In terms of an upper bound, we know that a handful of states supplement their food stamp and WIC programs; consequently, we could constrain our predictions such that the states with the highest propensity to spend on these programs would spend the current levels of federal funding plus the levels of state supplementation. More than likely, however, states will experience a decline in total financial effort directed at these programs relative to the status quo.

In addition, it is interesting to note that the Congressionally proposed swap bills do not include what can be considered an actual phase-in period. They do include a period during which the states and the federal government are held harmless, while state spending is bound by a maintenance of effort requirement. The actual change in financial burdens occurs abruptly -- there is no period where states are able to adjust to increasing levels of responsibility for the programs in question. Phase-ins may have not been a concern in drafting the legislation since the intent was for the changes to be budget neutral. However, the current proposals do not now appear to be budget neutral in the aggregate, and no such legislation is ever likely to be neutral from the perspective of individual states. The phase-in may be particularly important to the extent to which some programs tend to grow faster than others over time. As a consequence, easing the transition from current policy to a swap scenario through gradual phasing in of the changes should be considered a priority.

IV . Empirical Analysis of Alternative Swap Proposals

Any empirical analysis of swap proposals will be highly dependent upon the assumptions made about the likely responses of states to the new division of public responsibilities. As was

shown in the previous section, the magnitude of such responses are far from certain. The analysis presented here is intended to provide a range of possible spending outcomes resulting from a number of different swap proposals.¹⁹ The first part, referred to as the complete maintenance of effort case, will illustrate the effects of swaps in the purest and simplest form -- if states assume the current total levels of spending of devolved programs and the federal government continues current total levels of spending for federalized programs. The second part of the analysis uses a Medicaid-only swap proposal to demonstrate some possible results taking into account potential state responses. Both cases are based on 1993 data²⁰ and assume full phase-in of the proposals in fiscal year 1993.

Case 1: Complete Maintenance of Effort

As described above, many swap proposals represent a combination of practical or theoretical goals and adjustments to balance the aggregate numbers. Since these programs are of different sizes and not always easily subdivided, it is often difficult to achieve a budget neutral swap, even in the aggregate. Nonetheless, there are many different ways to potentially divide the programs we discuss here: Medicaid, AFDC, Food Stamps, WIC, and JOBS. These are the programs in Senator Nancy Kassebaum's original bill and they represent a logical place to start. At various times in the welfare debate, Aid to Families of Dependent Children (AFDC), the

¹⁹ Alice Rivlin's proposal is not included in this empirical analysis. The broad scope of the budgetary changes included in her plan (including comprehensive national reform of the health care financing system) make her proposal beyond the scope of this analysis.

²⁰ The level of Medicaid expenditures reported in this analysis is not likely to coincide with similar figures reported by the Health Care Financing Administration. The reason for this discrepancy can be attributed to several causes. First, the Urban Institute has developed a cross-walk between the HCFA 64 and HCFA 2082 data forms that results in a database more reflective of actual Medicaid spending. Second, the underlying data has been edited to correct for obvious errors in state reporting; these errors can be found in reported DSH payments and/or expenditures on certain services or eligibility groups. Finally, the numbers presented here do not include adjustments and collections, Arizona, or the US territories.

Special Supplemental Food Program for Women, Infants and Children (WIC), and food stamps have been mentioned as programs that might be combined in various ways, perhaps in block grants. The major AFDC related training program--the JOBS program--is also often grouped with these welfare benefits for consideration. As the other major means-tested program in the federal budget, Medicaid is also a logical piece of this puzzle. Table 1-A shows the state fiscal year 1993 expenditures for each of these programs under the current system. Table 1-B provides the fiscal year 1993 expenditures by the federal government for each state.

Tables 2 through 7 assume that spending levels on the various programs remain constant after the swap. While this is obviously not a realistic assumption, it is the simplest to model and at least represents a starting point for comparing impacts. In addition, any transition requirement would likely have a maintenance of effort clause which would at least begin the shifts of responsibility at approximately this level.

Senator Kassebaum's original bill offered a very simple swap arrangement: the federal government would assume Medicaid and the other four programs would revert to the states. This simple arrangement (described as swap number 1 in Table 2), however, would lead to a \$15.6 billion shortfall for the federal government (see Table 3A). In an environment in which the federal government is looking for ways to cut back on spending, such a proposal is likely to be deemed immediately unacceptable. The four biggest winning states in absolute dollars would be New York, New Jersey, Massachusetts, and California. And not surprisingly since the federal government would lose so much, there are few states that stand to lose under this scenario. New Mexico, Oklahoma and West Virginia would each lose over \$100 million. These states have Medicaid programs that are small relative to the other means tested programs. Regionally, the

Table 1-A
Current Program Spending
by State Government
(in millions of dollars)

	Current State Medicaid	Current State AFDC	Current State JOBS	Current State Food Stamps	Current State Total
United States	55,892.5	11,378.2	398.8	1,528.0	68,993.5
New England	4,473.3	790.5	20.4	54.5	5,338.8
Connecticut (*)	1,169.4	206.9	0.0	14.7	1,391.0
Maine	335.7	47.9	2.3	8.3	392.2
Massachusetts	2,075.0	419.2	10.1	21.3	2,515.6
New Hampshire	389.5	31.4	3.0	2.9	426.7
Rhode Island	393.1	85.3	3.8	5.4	487.7
Vermont	110.5	28.9	1.3	3.9	144.6
Middle Atlantic	15,122.2	2,411.0	97.7	287.5	17,898.3
New Jersey	2,423.0	342.1	16.0	51.4	2,834.4
New York	10,106.0	1,807.3	52.8	129.2	11,895.0
Pennsylvania	2,593.2	461.7	27.1	88.9	3,169.9
South Atlantic	7,854.3	1,287.5	49.5	240.3	9,221.5
Delaware	133.5	23.1	0.8	4.0	161.3
District of Columbia	354.9	70.3	2.5	8.3	436.0
Florida	2,293.9	424.8	4.3	80.7	2,783.7
Georgia	1,102.6	192.2	9.1	21.1	1,255.0
Maryland	1,029.2	164.2	8.5	47.7	1,249.6
North Carolina	1,020.5	149.3	11.9	32.4	1,214.1
South Carolina	604.4	43.3	2.2	17.7	667.7
Virginia	933.4	134.0	5.9	41.8	1,115.0
West Virginia	292.0	32.3	4.3	8.5	337.1
East South Central	2,172.8	231.4	18.8	95.7	2,520.4
Alabama	478.0	37.6	3.0	29.3	547.9
Kentucky	542.1	79.0	8.4	28.5	658.0
Mississippi	257.4	24.9	3.4	17.7	303.4
Tennessee	895.2	60.0	1.8	28.2	1,013.1
West South Central	4,280.2	375.3	37.8	195.8	4,879.2
Arkansas	273.3	21.8	1.1	14.1	310.3
Louisiana	997.5	56.6	7.5	34.4	1,096.2
Oklahoma	358.8	71.8	3.6	19.1	450.9
Texas	2,632.7	225.2	25.6	128.0	3,015.5
East North Central	8,888.1	1,832.7	78.5	231.4	10,810.7
Illinois	2,821.2	460.0	7.3	47.5	3,156.0
Indiana	1,052.4	103.2	5.6	24.5	1,185.7
Michigan	2,007.8	609.8	21.4	81.8	2,700.9
Ohio	2,123.5	441.9	30.7	71.9	2,668.0
Wisconsin	863.2	197.8	13.5	25.6	1,100.2
West North Central	3,108.3	515.4	27.8	79.2	3,728.6
Iowa	382.7	65.7	3.4	8.3	460.1
Kansas	385.4	83.3	8.9	7.5	485.6
Minnesota	1,030.3	201.8	8.5	26.4	1,266.0
Missouri	919.8	129.8	8.5	24.4	1,080.5
Nebraska	227.9	31.4	1.7	5.3	266.2
North Dakota	78.8	9.7	0.3	3.3	91.8
South Dakota	81.5	9.2	0.5	4.0	95.3
Mountain	1,237.3	219.0	8.6	52.1	1,517.0
Arizona (*)	n/a	n/a	n/a	n/a	n/a
Colorado	511.3	87.2	2.1	12.8	613.2
Idaho	90.9	12.4	1.4	4.1	108.7
Montana	87.8	18.8	1.6	5.3	113.5
Nevada	209.2	28.1	0.7	5.9	244.1
New Mexico	155.8	36.8	0.7	12.0	205.1
Utah	125.4	27.3	2.4	9.8	164.8
Wyoming	47.0	10.8	0.7	2.4	60.8
Pacific	8,995.0	3,729.6	59.0	307.6	13,091.3
Alaska	144.4	59.8	2.2	7.4	213.7
California	7,148.5	3,192.2	41.5	241.2	10,523.4
Hawaii	198.8	76.4	7.2	8.2	290.5
Oregon	381.4	95.2	3.9	17.3	507.8
Washington	1,104.9	306.1	5.3	33.7	1,449.9

Notes

Source of Medicaid data: Urban Institute adjustments to Health Care Financing Administration Medicaid 64 & 2002 data

Source of AFDC data: Overview of Entitlement Programs 1994 Green Book, Committee on Ways and Means, US House of

Representatives

Source of JOBS data: Department of Health & Human Services, Office of Family Assistance, JOBS Information and Measurement

Branch (MIS 3/9/95)

Source of Food Stamps data: Food and Nutrition Service, National Data Bank

Source of WIC data: Food and Nutrition Service, Program Information Division/PIAB

(*) Current spending by the state of Connecticut on the JOBS program was unavailable. It is shown here as zero.

(**) The state of Arizona is excluded from the analysis in this work because its reported Medicaid data is not comparable with reporting by the other states.

8/5/95 14.08

Table 1-8

Current Program Spending
by the Federal Government
(in millions of dollars)

	Current Federal Medicaid	Current Federal AFDC	Current Federal JOBS	Current Federal Food Stamps	Current Federal WIC	Current Federal Total
United States	74,178.8	13,485.9	719.3	23,194.6	2,858.3	114,234.7
New England	4,797.1	841.0	41.0	795.4	122.8	6,567.0
Connecticut	1,189.4	206.9	8.1	158.1	34.8	1,576.4
Maine	543.4	75.8	3.7	118.4	12.8	753.7
Massachusetts	2,075.0	410.2	21.1	348.7	47.0	2,902.0
New Hampshire	389.5	31.4	2.3	49.1	9.2	481.4
Rhode Island	454.9	75.1	4.6	78.7	10.7	624.2
Vermont	165.0	41.8	2.9	42.4	8.3	260.4
Middle Atlantic	15,769.8	2,513.5	136.4	3,502.4	381.0	22,292.0
New Jersey	2,423.0	342.1	27.0	517.7	56.8	3,368.8
New York	10,106.0	1,607.3	80.3	1,832.9	209.5	13,936.0
Pennsylvania	3,231.8	562.2	29.2	1,051.8	111.8	4,986.4
South Atlantic	11,228.4	1,879.4	92.2	4,199.9	454.7	17,645.5
Delaware	133.5	23.1	1.8	50.7	7.2	216.0
District of Columbia	354.9	70.3	4.7	89.4	8.1	527.3
Florida	2,807.1	505.7	16.4	1,400.8	107.5	4,836.4
Georgia	1,605.1	296.8	15.7	708.2	87.6	2,613.3
Maryland	1,029.2	194.2	13.4	354.7	38.3	1,631.8
North Carolina	1,070.9	281.8	17.7	514.1	73.5	2,841.0
South Carolina	1,251.9	90.8	4.8	324.8	54.2	1,726.1
Virginia	933.4	138.0	9.4	477.2	58.7	1,613.6
West Virginia	936.4	96.3	9.5	268.4	23.4	1,337.0
East South Central	5,404.0	491.1	38.6	2,013.4	209.2	8,158.4
Alabama	1,198.2	76.5	9.0	469.3	54.4	1,830.5
Kentucky	1,372.5	170.0	13.7	450.1	51.7	2,058.1
Mississippi	969.0	75.3	6.9	435.9	41.9	1,532.0
Tennessee	1,885.2	187.2	6.0	639.2	57.3	2,764.9
West South Central	9,161.8	713.8	85.6	3,605.1	385.1	13,631.1
Arkansas	794.8	50.9	9.0	224.2	36.5	1,111.6
Louisiana	2,796.8	140.8	18.5	890.2	87.8	3,717.1
Oklahoma	616.1	136.2	8.5	314.1	40.4	1,319.4
Texas	4,770.9	385.9	37.5	2,378.8	220.4	7,786.4
East North Central	11,504.6	2,324.1	147.7	3,873.1	418.8	18,265.9
Illinois	2,621.2	440.0	24.3	1,112.0	106.7	4,348.2
Indiana	1,808.1	182.8	9.1	432.5	59.2	2,471.5
Michigan	2,536.8	748.9	35.2	702.8	88.8	4,314.5
Ohio	3,218.6	642.9	58.7	1,178.6	114.3	5,211.1
Wisconsin	1,317.7	236.7	20.4	249.1	45.8	1,922.6
West North Central	4,589.3	711.1	39.1	1,238.6	181.5	6,757.6
Iowa	544.5	111.3	5.9	155.6	28.2	843.5
Kansas	536.2	64.4	8.4	149.4	24.8	801.3
Minnesota	1,255.7	239.7	11.8	255.4	39.2	1,801.8
Missouri	1,394.8	188.0	9.8	503.8	54.7	2,151.1
Nebraska	381.3	49.2	2.7	88.4	15.8	512.3
North Dakota	204.1	22.1	1.3	39.2	9.2	278.0
South Dakota	192.7	19.4	1.3	46.8	11.7	271.9
Mountain	2,220.5	373.4	21.5	795.2	117.4	3,528.0
Arizona (*)	n/a	n/a	n/a	n/a	n/a	n/a
Colorado	810.4	101.6	8.1	240.0	27.8	987.8
Idaho	224.8	24.4	2.3	59.3	15.8	328.3
Montana	238.5	30.4	2.5	81.0	10.4	360.1
Nevada	229.2	28.2	1.2	92.0	9.8	360.4
New Mexico	439.8	83.5	1.5	206.7	23.9	765.1
Utah	382.2	66.7	4.6	107.4	23.7	584.5
Wyoming	95.8	19.8	1.4	28.8	8.1	151.6
Pacific	9,492.5	3,840.5	137.4	3,182.5	408.3	17,061.2
Alaska	144.4	59.8	1.6	52.8	8.7	267.7
California	7,148.5	3,192.2	99.5	2,332.8	313.9	13,688.9
Hawaii	198.8	79.4	4.1	140.8	15.5	435.4
Oregon	649.2	145.4	11.4	251.1	28.2	1,087.3
Washington	1,351.8	386.8	20.6	403.5	42.0	2,184.5

Notes

Source of Medicaid data: Urban Institute adjustments to Health Care Financing Administration Medicaid 64 & 2062 data.

Source of AFDC data: Overview of Entitlement Programs: 1994 Green Book, Committee on Ways and Means, US House of Representatives.

Source of JOBS data: Department of Health & Human Services, Office of Family Assistance, JOBS Information and Measurement Branch (MIS, 3/5/95).

Source of Food Stamps data: Food and Nutrition Service, National Data Bank.

Source of WIC data: Food and Nutrition Service, Program Information Division/PRA/B.

(*) The state of Arizona is excluded from the analysis in this work because its reported Medicaid data is not comparable with reporting by the other states.

8/5/95 14 07

Table 2

Descriptions of Swaps:	Swap #1	Swap #2	Swap #3	Swap #4	Swap #5
State Assumes:	AFDC, Food Stamps, WIC, JOBS	AFDC, Food Stamps, WIC, JOBS, Acute and Long Term Care Medicaid for Adults & Kids, DSH, Medicaid Payments to HMOs	AFDC, JOBS, Acute and Long Term Care Medicaid for Adults & Kids, DSH, Medicaid Payments to HMOs	AFDC, Food Stamps, WIC, JOBS, Optional Medicaid Benefits, DSH	AFDC, WIC, JOBS, Optional Medicaid Benefits, DSH
Federal Government Assumes:	Full Medicaid	Acute and Long Term Care Medicaid for the Aged & Disabled	Acute and Long Term Care Medicaid for the Aged & Disabled, Food Stamps, WIC	Full Medicaid Less Optional Benefits and DSH	Full Medicaid Less Optional Benefits and DSH, Food Stamps

Notes

Medicaid administrative costs are distributed between the states and federal governments in proportion to their shares of Medicaid benefit dollars

Medicaid Payments to HMOs are shown here as a separate line item because the data do not allow differentiation of these payments by population group. The payments are attributable to acute care for adults and children and would, under an actual policy change, be allocated to the level of government responsible for the relevant population group

Table 3A

Static Model Results: Affect of Alternative Swaps on FY 1993 State Finances
(dollars in millions)

State	Change in Liability: Swap #1	Change in Liability: Swap #2	Change in Liability: Swap #3	Change in Liability: Swap #4	Change in Liability: Swap #5
United States	-15,636.4	37,668.7	10,309.8	18,967.4	-5,755.2
New England	-2,673.4	785.1	-187.4	-5.0	-854.9
Connecticut	-763.5	54.8	-152.8	-131.6	-304.4
Maine	-125.4	205.9	68.8	183.8	59.1
Massachusetts	-1,248.0	277.5	-139.5	-271.9	-642.0
New Hampshire	-297.6	190.7	129.6	168.0	116.0
Rhode Island	-223.9	-9.9	-104.7	-19.3	-103.4
Vermont	-15.1	66.1	11.5	66.0	19.7
Middle Atlantic	-8,590.9	2,351.0	-1,799.8	-178.0	-3,945.8
New Jersey	-1,476.5	842.2	13.3	114.2	-454.8
New York	-6,276.1	249.3	-2,022.3	-841.6	-2,906.6
Pennsylvania	-838.3	1,459.6	209.2	554.4	-584.4
South Atlantic	-1,247.2	6,624.5	1,738.6	3,090.8	-1,340.4
Delaware	-51.0	25.2	-36.6	-11.0	-70.6
District of Columbia	-182.4	57.7	-48.1	-60.3	-156.0
Florida	-264.6	1,867.9	299.0	898.0	-763.3
Georgia	5.7	1,318.9	475.2	725.6	-30.3
Maryland	-426.6	357.2	-58.9	-205.9	-585.8
North Carolina	-153.3	1,145.6	525.6	550.6	4.1
South Carolina	-27.3	848.0	451.6	714.2	372.0
Virginia	-253.2	376.8	-197.9	135.0	-383.0
West Virginia	105.6	827.0	328.8	549.5	274.6
East South Central	579.5	3,891.8	1,569.5	2,689.1	776.0
Alabama	156.2	935.8	359.8	847.6	330.0
Kentucky	143.4	883.0	354.8	629.4	152.8
Mississippi	305.5	801.7	306.2	625.0	171.5
Tennessee	-25.5	1,271.3	548.8	787.0	121.7
West South Central	489.3	7,193.5	3,027.7	5,076.7	1,275.9
Arkansas	43.4	325.9	51.0	218.2	-20.1
Louisiana	-82.6	1,906.1	1,113.8	1,548.5	823.9
Oklahoma	143.7	593.0	219.3	316.9	-16.2
Texas	384.8	4,368.6	1,643.5	2,993.0	488.4
East North Central	-1,906.8	5,644.2	1,123.2	1,946.4	-2,158.1
Illinois	-896.2	929.6	-338.5	-122.8	-1,282.3
Indiana	-389.0	849.7	333.5	20.0	-437.0
Michigan	-232.1	1,717.3	663.8	997.5	32.9
Ohio	-131.0	1,909.2	546.3	897.9	-350.6
Wisconsin	-258.3	238.5	-81.9	153.7	-121.1
West North Central	-938.0	1,873.8	376.5	902.5	-413.3
Iowa	-83.7	235.4	45.4	67.1	-96.7
Kansas	-120.3	299.1	117.4	184.4	27.5
Minnesota	-484.5	171.8	-149.1	-244.2	-526.0
Missouri	-163.5	952.1	369.1	82.2	294.9
Nebraska	-76.8	98.9	-8.5	15.4	-76.3
North Dakota	-6.7	57.3	5.5	26.8	-15.8
South Dakota	-2.4	59.2	-3.3	29.8	-21.0
Mountain	70.2	1,486.8	522.1	790.7	-56.6
Arizona	n/a	n/a	n/a	n/a	n/a
Colorado	-134.0	321.0	40.7	130.5	-122.1
Idaho	12.6	105.4	24.6	71.2	6.1
Montana	13.8	132.0	57.0	72.2	7.7
Nevada	-78.0	140.8	33.0	44.2	-53.8
New Mexico	169.9	405.7	183.0	280.1	81.4
Utah	76.9	316.0	175.1	165.7	46.6
Wyoming	9.0	65.9	28.6	26.7	-4.5
Pacific	-1,419.2	7,838.0	3,939.4	4,452.3	962.0
Alaska	-21.6	155.0	86.4	71.1	11.2
California	-1,210.1	6,353.8	3,465.9	3,520.8	946.8
Hawaii	37.7	207.0	42.6	130.2	-16.6
Oregon	46.7	427.9	129.4	270.3	0.0
Washington	-272.0	694.3	215.1	459.9	22.7

Note: A negative number indicates a decrease in state expenditures and an increase in federal expenditures

Table 3B

Static Model Results: Affect of Alternative Swaps on FY 1993 State Finances
(Percentage Change from Current System)

State	% Change in Liability: Swap #1	% Change in Liability: Swap #2	Change in Liability: Swap #3	% Change in Liability: Swap #4	Change in Liability: Swap #5
United States	-22.7%	54.6%	14.9%	27.5%	-8.3%
New England	-50.1%	14.7%	-3.5%	-0.1%	-16.0%
Connecticut	-54.9%	3.9%	-11.0%	-9.5%	-21.9%
Maine	-32.0%	52.5%	17.5%	46.9%	15.1%
Massachusetts	-49.6%	11.0%	-5.5%	-10.8%	-25.5%
New Hampshire	-69.7%	44.7%	30.4%	39.4%	27.2%
Rhode Island	-47.9%	-2.1%	-22.4%	-4.1%	-22.1%
Vermont	-10.4%	45.7%	8.0%	45.6%	13.6%
Middle Atlantic	-48.0%	13.1%	-10.1%	-1.0%	-22.0%
New Jersey	-52.1%	22.7%	0.5%	4.0%	-16.0%
New York	-52.8%	2.1%	-17.0%	-7.1%	-24.4%
Pennsylvania	-26.5%	46.1%	6.6%	17.5%	-18.4%
South Atlantic	-13.5%	71.8%	18.9%	35.5%	-14.5%
Delaware	-31.8%	15.6%	-22.7%	-9.9%	-43.8%
District of Columbia	-41.8%	13.2%	-11.0%	-13.8%	-36.2%
Florida	-9.5%	67.1%	10.7%	25.1%	-27.4%
Georgia	0.4%	97.6%	35.2%	53.7%	-2.2%
Mayland	-34.0%	28.5%	-4.7%	-16.4%	-46.7%
North Carolina	-12.6%	94.4%	43.3%	45.3%	0.3%
South Carolina	-4.8%	149.4%	79.6%	125.8%	65.5%
Virginia	-22.6%	33.7%	-17.7%	12.1%	-34.2%
West Virginia	31.5%	187.1%	98.1%	164.0%	81.9%
East South Central	23.0%	154.4%	62.3%	114.6%	30.8%
Alabama	23.5%	170.8%	65.7%	154.7%	60.2%
Kentucky	21.9%	134.6%	54.1%	96.0%	23.3%
Mississippi	100.7%	264.2%	100.9%	206.0%	56.5%
Tennessee	-2.5%	125.5%	54.2%	77.7%	12.0%
West South Central	10.0%	147.6%	62.1%	104.2%	26.2%
Arkansas	14.0%	105.0%	16.4%	70.3%	4.5%
Louisiana	-7.5%	173.9%	101.6%	141.3%	75.2%
Oklahoma	31.9%	131.5%	46.6%	70.3%	-3.6%
Texas	12.8%	144.9%	54.5%	99.3%	16.2%
East North Central	-17.6%	52.2%	10.4%	18.0%	-20.0%
Illinois	-28.4%	29.5%	-10.7%	-3.9%	-40.6%
Indiana	-32.8%	71.7%	28.1%	1.7%	-36.9%
Michigan	-8.6%	63.6%	24.6%	36.9%	1.2%
Ohio	-4.9%	71.6%	20.5%	33.7%	-13.1%
Wisconsin	-23.5%	21.7%	-7.4%	14.0%	-11.0%
West North Central	-25.2%	52.7%	10.0%	24.3%	-12.5%
Iowa	-18.0%	50.7%	9.8%	14.5%	-20.8%
Kansas	-25.8%	64.2%	25.2%	39.6%	5.9%
Minnesota	-38.3%	13.6%	-11.8%	-19.3%	-41.6%
Missouri	-15.1%	88.1%	34.2%	76.2%	27.3%
Nebraska	-28.9%	37.1%	-3.2%	5.8%	-28.7%
North Dakota	-7.3%	62.3%	6.0%	29.1%	17.2%
South Dakota	-2.5%	62.2%	-3.5%	31.3%	-22.0%
Mountain	4.6%	98.0%	34.4%	52.1%	-3.7%
Arizona	n/a	n/a	n/a	n/a	n/a
Colorado	-21.8%	52.3%	6.6%	21.3%	-19.9%
Idaho	11.6%	97.0%	22.8%	65.4%	5.6%
Montana	11.2%	106.9%	46.2%	58.5%	6.3%
Nevada	-32.2%	58.2%	13.6%	18.3%	-22.2%
New Mexico	82.9%	197.8%	79.5%	136.6%	29.9%
Utah	46.7%	191.7%	106.3%	100.5%	29.5%
Wyoming	14.8%	108.9%	47.3%	44.1%	-7.4%
Pacific	-10.6%	59.9%	30.1%	34.0%	7.4%
Alaska	-16.1%	72.9%	40.8%	33.4%	5.3%
California	-11.4%	59.8%	32.6%	33.1%	8.9%
Hawaii	13.0%	71.2%	14.7%	44.8%	-6.4%
Oregon	9.2%	84.3%	25.5%	53.2%	0.0%
Washington	-18.8%	47.9%	14.6%	31.7%	1.6%

Note: A negative percentage indicates a decrease in state expenditures and an increase in federal expenditures.

8/11/95 16:16

Middle Atlantic is the largest gainer and East South and West South Central loses. The Mountain states lose to a small degree.

But because the size of the states differ substantially, it is important to normalize the results by looking at them in terms of percentages changes compared to the current system. This is shown in Table 3B. In this case, the New England region is actually the biggest gainer at 50.1 percent (as compared to the Middle Atlantic at 48 percent). And the East South Central loses more as a share of the current system (23 percent) as compared to the Mountain states (4.6 percent). New Hampshire and Connecticut are the largest relative gainers and Mississippi is the biggest losing state as a percentage share.

It is important to note, moreover, that these various programs are not likely to grow at the same rates over time. Medicaid has grown much faster than the cash programs over time, suggesting yet another reason why it might be unacceptable to take on more liability in the first year by federalizing Medicaid. That disparity is likely to grow over time rather than diminish.

As a first pass at how the original Kassebaum swap proposal might be modified, the remaining four options (described in Table 2 and results in Tables 3A and 3B) each shift part of Medicaid's responsibilities to the states. And in swap 3, WIC and food stamps remain at the federal level while in swap 5, food stamps remains a federal responsibility.

Swap number 2 would federalize that portion of Medicaid which benefits the elderly and disabled, including both long term and acute care services. Since Social Security and Medicare are federal programs which serve the elderly and disabled, it makes sense to group together populations in this way. Similarly, the states would thus have full responsibility for younger families. (For ease of presentation, the states also retain the full food stamp program, although

some of the benefits under that program do go to elderly and disabled persons.) In this case, states would become major losers, taking on an additional \$37.7 billion in responsibilities if there were a full maintenance of effort. California would now lead the list of losers in dollar terms (Table 3A) followed by Texas. Both of these states have relatively small long term care programs and hence do not benefit as much as others from this change. The only state which wins under this option would be Rhode Island--and then by only \$10 million, or 2.1 percent. The largest percentage losing states would be Mississippi, New Mexico, Utah, and West Virginia--all having more than a 190 percent increase in their burdens. Not unexpectedly, then, there are no regional winners. The Pacific states would lose the most in dollars, but the largest percentage loser would be the East South Central region.

Swap 3 keeps the same Medicaid breakdown (elderly and disabled spending at the federal level) as swap 2, but also retains food stamps and WIC at the federal level. This reduces state losses by over \$27 billion in 1993 dollars relative to swap 2. California's loss is cut almost in half and Texas' loss drops even further. A number of states switch to the winning category including New York which would gain by over \$2 billion. This variation also reduces substantially the variability in winners and losers by region in dollar terms. Viewed in percentages, the region with the greatest loss is the East South Central at 62.3 percent--much lower than under swap 2. Only the Middle Atlantic and New England regions gain. Rhode Island is the biggest percentage gainer and Utah the largest loser.

This gap widens again under swap number 4 in which only optional benefits and disproportionate share payments (DSH) are returned to states. The logic for this approach rests with the fact that states have a lot of discretion in terms of these two areas. They can

substantially raise the size of their programs by using these services. DSH is particularly an area that states have used to their own advantage and some have gone beyond the legislative intent. States are still losers, but by only \$19 billion (using 1993 numbers). California and Texas remain big losers, and Louisiana is also a major loser as well, by nearly as much as under swap number 2. Louisiana depends very heavily on the disproportionate share program, helping to explain why the West South Central is the largest loser among the regions. Several states would gain under this option, however, including New York, Massachusetts, Minnesota and Maryland. On a regional basis, the Middle Atlantic is the winner--due totally to New York state's gains.

On a percentage basis, losses in the East South Central are the largest, due to losses of 206 percent and 154.7 percent by Mississippi and Alabama respectively. Only New England and the Middle Atlantic are winners by this measure, by 1 percent or less. And the biggest winning state is Minnesota.

Swap 5 results in a federal loss and state gain at the aggregate level. It is the only other option presented besides Kassebaum's original approach to do so. The federal government would retain food stamps and all of Medicaid except DSH and optional benefits. As noted above, DSH and optional benefits are both essentially optional programs, so returning them to the state level makes considerable sense. Moreover, since food stamps is now a federal program, this allocation could be readily justified. It also helps to limit the number of losing states since on aggregate the federal government takes on more responsibilities. After New York, Illinois is the biggest gainer from this option in dollars, and the Middle Atlantic is the biggest winner regionally. The West South Central and the states of California, Louisiana and Texas are big losers. By percentages, the Middle Atlantic and the East North Central are nearly equal winners.

Table 4

Descriptions of Swaps:	Swap #6	Swap #7	Swap #8	Swap #9
State Assumes:	AFDC; Food Stamps; WIC; JOBS; Acute Care Medicaid for Adults, Kids, Disabled & Non-Medicare Aged; DSH; Medicaid Payments to HMOs	AFDC; JOBS; Acute Care Medicaid for Adults, Kids, Disabled & Non-Medicare Aged; DSH; Medicaid Payments to HMOs	AFDC; Food Stamps; WIC; JOBS; All Medicaid Long Term Care; Optional Medicaid Benefits (not including drugs); DSH	AFDC; JOBS; All Medicaid Long Term Care; Optional Medicaid Benefits (not including drugs); DSH
Federal Government Assumes:	All Medicaid Long Term Care; Acute Care Medicaid for Aged Medicare	All Medicaid Long Term Care; Acute Care Medicaid for Aged Medicare; Food Stamps; WIC	All Medicaid Mandatory Acute Care; Medicaid Drugs	All Medicaid Mandatory Acute Care; Medicaid Drugs; Food Stamps; WIC

Notes:

Medicaid administrative costs are distributed between the states and federal governments in proportion to their shares of Medicaid benefit dollars.

Medicaid Payments to HMOs are shown here as a separate line item because the data do not allow differentiation of these payments by population group. The payments are attributable to acute care for adults and children and would, under an actual policy change, be allocated to the level of government responsible for the relevant population group.

Table 5A

Static Model Results: Affect of Alternative Swaps on FY 1993 State Finances
(dollars in millions)

State	Change in Liability: Swap #6	Change in Liability Swap #7	Change in Liability Swap #8	Change in Liability Swap #9
United States	65,531.0	36,152.1	57,596.2	30,217.3
New England	2,418.8	1,446.4	3,596.9	2,624.4
Connecticut	288.6	81.0	975.9	768.3
Maine	377.3	240.1	493.7	356.5
Massachusetts	1,177.4	760.4	1,216.7	799.7
New Hampshire	240.4	179.3	378.9	317.8
Rhode Island	201.5	106.6	365.5	270.7
Vermont	133.7	79.1	166.2	111.5
Middle Atlantic	8,582.3	4,431.5	11,942.4	7,791.6
New Jersey	1,628.6	1,000.0	1,546.6	917.7
New York	4,897.6	2,426.0	7,555.3	5,283.8
Pennsylvania	2,255.9	1,005.5	2,840.5	1,590.1
South Atlantic	11,178.7	6,292.8	7,797.3	2,911.4
Delaware	96.8	35.0	86.3	24.5
District of Columbia	250.0	144.1	188.9	83.1
Florida	3,157.6	1,588.7	1,764.3	195.4
Georgia	2,048.8	1,205.1	1,307.7	464.0
Maryland	955.6	539.7	331.8	-84.4
North Carolina	1,624.7	1,004.7	1,516.8	896.6
South Carolina	1,206.4	810.0	1,106.8	710.4
Virginia	865.3	290.6	884.7	110.0
West Virginia	973.2	674.9	810.0	511.7
East South Central	5,775.7	3,453.4	4,407.4	2,085.1
Alabama	1,273.7	697.7	1,226.6	650.8
Kentucky	1,463.2	934.9	1,014.2	486.0
Mississippi	1,128.2	630.7	837.9	342.4
Tennessee	1,912.7	1,190.1	1,328.8	606.2
West South Central	9,757.2	5,591.4	8,206.0	4,040.2
Arkansas	593.2	318.3	627.8	352.9
Louisiana	2,711.0	1,918.7	2,296.5	1,504.2
Oklahoma	746.7	373.1	766.4	392.8
Texas	5,706.4	2,981.3	4,515.3	1,790.2
East North Central	9,963.3	5,442.3	6,860.2	4,159.2
Illinois	2,318.9	1,050.7	1,483.2	215.1
Indiana	1,346.6	830.5	948.5	432.4
Michigan	2,717.7	1,564.3	2,312.2	1,258.8
Ohio	2,658.9	1,496.1	2,826.6	1,463.7
Wisconsin	721.1	400.7	1,109.7	789.3
West North Central	3,042.8	1,545.4	3,898.3	2,401.0
Iowa	418.3	228.2	438.0	247.9
Kansas	405.6	223.9	504.0	322.2
Minnesota	401.2	80.2	1,040.7	719.8
Missouri	1,372.3	789.4	1,331.9	748.9
Nebraska	215.9	108.5	245.9	138.5
North Dakota	105.9	54.2	180.6	128.8
South Dakota	123.6	81.1	157.3	94.8
Mountain	2,226.3	1,261.7	1,855.7	891.0
Arizona	n/a	n/a	n/a	n/a
Colorado	576.6	296.4	474.9	194.7
Idaho	187.6	106.8	185.9	105.0
Montana	180.0	105.1	211.2	136.2
Nevada	228.6	120.8	156.6	48.8
New Mexico	559.0	316.4	445.7	203.0
Utah	406.6	265.8	303.8	162.9
Wyoming	87.9	50.6	77.6	40.3
Pacific	12,585.8	6,687.2	7,211.9	3,313.3
Alaska	203.1	134.5	118.7	50.1
California	10,289.6	7,401.7	4,902.9	2,015.0
Hawaii	297.5	133.2	234.8	70.5
Oregon	802.5	303.9	675.9	377.3
Washington	1,193.1	713.9	1,279.6	800.4

Note: A negative number indicates a decrease in state expenditures and an increase in federal expenditures

Table 5B

Static Model Results: Affect of Alternative Swaps on FY 1993 State Finances
(Percentage Change from Current System)

State	% Change in Liability: Swap #6	Change in Liability: Swap #7	% Change in Liability: Swap #8	Change in Liability: Swap #9
United States	95.0%	55.3%	83.5%	43.8%
New England	45.3%	27.1%	67.4%	49.2%
Connecticut	20.7%	5.8%	70.2%	55.2%
Maine	96.2%	61.2%	125.9%	90.9%
Massachusetts	46.8%	30.2%	48.3%	31.8%
New Hampshire	56.3%	42.0%	88.8%	74.5%
Rhode Island	43.1%	22.8%	78.2%	57.9%
Vermont	92.4%	54.7%	114.9%	77.1%
Middle Atlantic	48.0%	24.8%	66.7%	43.5%
New Jersey	57.5%	35.3%	54.6%	32.4%
New York	39.5%	20.4%	63.5%	44.4%
Pennsylvania	71.2%	31.7%	89.6%	50.2%
South Atlantic	121.2%	68.2%	84.6%	31.6%
Delaware	60.0%	21.7%	53.5%	15.2%
District of Columbia	57.3%	33.1%	43.3%	19.1%
Florida	113.4%	57.1%	63.4%	7.0%
Georgia	151.6%	89.2%	96.8%	34.3%
Maryland	76.3%	43.1%	26.5%	-6.7%
North Carolina	133.8%	82.8%	124.9%	73.9%
South Carolina	212.5%	142.7%	195.0%	125.1%
Virginia	77.3%	26.0%	61.2%	9.8%
West Virginia	290.4%	201.4%	241.7%	152.7%
East South Central	229.2%	137.0%	174.9%	82.7%
Alabama	232.5%	127.3%	223.9%	118.7%
Kentucky	223.1%	142.5%	154.6%	74.1%
Mississippi	371.1%	207.8%	276.1%	112.8%
Tennessee	168.8%	117.5%	131.2%	59.8%
West South Central	200.2%	114.7%	168.4%	82.9%
Arkansas	191.2%	102.6%	202.3%	113.7%
Louisiana	247.3%	175.0%	209.5%	137.2%
Oklahoma	165.6%	82.7%	170.0%	87.1%
Texas	189.2%	98.9%	149.7%	59.4%
East North Central	92.2%	50.3%	80.3%	38.5%
Illinois	73.5%	33.3%	47.0%	6.8%
Indiana	113.8%	70.0%	80.0%	36.5%
Michigan	100.6%	61.6%	85.6%	46.6%
Ohio	107.2%	56.1%	105.9%	54.9%
Wisconsin	65.5%	36.4%	100.9%	71.7%
West North Central	81.6%	41.4%	104.6%	64.4%
Iowa	90.1%	49.2%	94.4%	53.4%
Kansas	87.1%	48.1%	108.2%	69.2%
Minnesota	31.7%	6.3%	82.3%	56.9%
Missouri	127.0%	73.1%	123.3%	69.3%
Nebraska	81.1%	40.8%	92.4%	52.0%
North Dakota	115.3%	59.0%	196.6%	140.3%
South Dakota	129.7%	64.1%	165.2%	99.5%
Mountain	146.7%	83.1%	122.3%	58.7%
Arizona	n/a	n/a	n/a	n/a
Colorado	94.0%	48.3%	77.5%	31.8%
Idaho	172.8%	98.2%	170.9%	96.6%
Montana	145.9%	65.1%	171.1%	110.4%
Nevada	94.4%	49.9%	64.7%	20.2%
New Mexico	272.6%	154.3%	217.3%	99.0%
Utah	246.7%	161.3%	184.3%	98.9%
Wyoming	145.0%	83.5%	128.2%	66.6%
Pacific	96.2%	66.4%	55.1%	25.3%
Alaska	95.5%	63.2%	55.8%	23.6%
California	96.9%	69.7%	46.2%	19.0%
Hawaii	102.4%	45.8%	80.8%	24.3%
Oregon	118.7%	59.9%	133.1%	74.3%
Washington	82.3%	49.2%	88.3%	55.2%

Note: A negative percentage indicates a decrease in state expenditures and an increase in federal expenditures.

A 30.8 percent loss makes the East South Central the biggest loser.

Swap number 6 (shown in Tables 4, 5A and 5B) leaves the responsibility for all long term care--including that for children--as well as Medicaid coverage for elderly Medicare recipients with the federal government. Thus, while the federal government would cover long term care for children and other adults, the states would have to pay for acute care for the disabled, a very expensive population to cover. This option results in the highest level of state burdens in aggregate of all the tables. California's loss rises to \$10.3 billion. Texas, New York and Florida constitute the next three largest losers. The South Atlantic and Pacific regions would each lose over \$11 billion. Under this scenario no state would gain, at least initially. As seen in Table 5B, the U.S. average change would be nearly a doubling of state burdens. Four of the regions' burdens would more than double. The East South Central region would experience a 229.2 percent increase in burdens.

Swap number 8 results in slightly lower state losses as compared to swap 6, but with a very different set of Medicaid changes. All mandatory acute services and prescription drug coverage becomes the responsibility of the federal government. Everything else reverts to the states. Although all states are losers (because of the high aggregate losses), those with large long term care programs relative to the rest of their Medicare programs are the greatest losers. That is, New York is now the main loser, passing California (as compared to swap 6). And, as usual, Texas is also a loser. The largest percentage losses are felt by the East South Central and West South Central regions and Mississippi tops the list as a percentage loser.

By making food stamps and WIC the responsibility of the federal government under swaps 7 and 9 (as compared to swaps 6 and 8), state losses are reduced but still remain at what

would likely be an unacceptably high level. The patterns of winners and losers remain stable between the original and modified options; the losses are simply lower. The exception is for swap 9 and Maryland, which actually gains under this option. In addition, losses are substantially reduced under swap 9 for Illinois and Florida.

The last set of options shown in Tables 6 and 7 attempts to leave the aggregate shares relatively even between states and the federal government. While there is still substantial variation across states, these combinations at least are relatively true to the concept of a "swap" as opposed to a shifting of funding burdens. The exception is swap 14, which is the revised version of the Kassebaum bill. Ironically, the modification made by Kassebaum resulted in more than a \$50 billion differential in burdens -- from a \$15.6 billion federal loss in swap 1 to a \$36.2 billion federal gain.

As described in Tables 6, 7A and 7B, swap 10 essentially federalizes Medicaid for children, the elderly and the disabled and leaves medical care for adults to the states. This makes some logical sense but it does effectively break up families between federal and state programs. DSH becomes a federal program, as does WIC. Its chief advantage is that it is the most nearly budget neutral. But interestingly, there is considerable variation among states. New York is a greater winner here than in all other swaps except for the original Kassebaum proposal. Mississippi is a major loser in percentage terms, helping to bring down the East South Central. The New England and Middle Atlantic regions are the major gainers as a share of current burdens.

Swap 11 retains all of Medicaid except optional benefits at the federal level. Thus, it is one of the simplest options to explain and perhaps to administer. States lose in aggregate, but by

Table 6

Descriptions of Swaps:	Swap #10	Swap #11	Swap #12	Swap #13	Swap #14 (S. 707)
State Assumes:	AFDC; Food Stamps; JOBS; Acute and Long Term Care Medicaid for Adults; Medicaid Payments to HMOs	AFDC; Food Stamps; WIC; JOBS; Optional Medicaid Benefits	AFDC; Food Stamps; WIC; JOBS; Acute Care Medicaid for Adults; Medicaid payments to HMOs;	AFDC; JOBS; All Medicaid Long Term Care	AFDC; JOBS; Food Stamps; WIC; DSH; Medicaid Payments to HMOs; Kids & Adults Acute Care Medicaid
Federal Government Assumes:	Acute and Long Term Care Medicaid for the Aged & Disabled and Kids; DSH; WIC	Full Medicaid (including DSH) less Optional Benefits	All Medicaid Long Term Care; Acute Care Medicaid for Aged & Disabled & Kids; DSH	All Medicaid Mandatory and Optional Acute Care (including drugs); DSH; Food Stamps; WIC	All long term care; Medicaid acute care for elderly & disabled

Notes:

Medicaid administrative costs are distributed between the states and federal governments in proportion to their shares of Medicaid benefit dollars.

Medicaid Payments to HMOs are shown here as a separate line item because the data do not allow differentiation of these payments by population group. The payments are attributable to acute care for adults and children and would, under an actual policy change, be allocated to the level of government responsible for the relevant population group.

Table 7A

Static Model Results: Affect of Alternative Swaps on FY 1993 State Finances
(dollars in millions)

State	Change in Liability Swap #10	Change in Liability Swap #11	Change in Liability Swap #12	Change in Liability Swap #13	Change in Liability Swap #14 (\$ 707)
United States	358.2	1,414.3	2,308.9	2,790.1	36,241.7
New England	-1,793.5	-1,810.5	-1,710.9	324.9	655.2
Connecticut	-638.7	-560.1	-615.5	225.8	0.2
Maine	-61.1	14.3	-51.8	91.3	193.0
Massachusetts	-567.9	-769.1	-632.8	-12.1	246.8
New Hampshire	-260.7	-223.0	-253.9	-128.2	177.6
Rhode Island	-176.7	-118.7	-173.6	95.1	-25.4
Vermont	11.6	46.0	18.5	51.1	62.9
Middle Atlantic	-5,884.9	-4,773.2	-6,619.1	872.0	2,052.6
New Jersey	-955.9	-1,006.4	-910.3	-414.0	588.8
New York	-4,793.7	-3,479.4	-4,664.0	544.7	133.0
Pennsylvania	-135.3	-267.4	-44.8	541.3	1,330.8
South Atlantic	1,234.2	1,325.9	1,567.8	-254.2	6,445.4
Delaware	-28.2	-21.5	-23.8	2.5	23.0
District of Columbia	-102.9	-101.9	-97.9	-18.1	51.7
Florida	418.6	451.0	501.9	-414.8	1,854.4
Georgia	483.2	404.2	553.8	-60.5	1,311.1
Maryland	-86.6	-287.6	-61.8	-207.7	339.7
North Carolina	219.4	193.3	268.6	356.2	1,072.1
South Carolina	104.9	254.1	148.3	60.8	833.5
Virginia	-78.7	-1.2	-34.2	-116.9	362.3
West Virginia	304.3	441.4	312.9	144.3	597.7
East South Central	1,363.2	1,719.8	1,535.3	375.4	3,790.4
Alabama	266.7	419.0	320.7	83.5	931.0
Kentucky	393.3	488.6	434.7	167.8	846.8
Mississippi	427.8	468.9	464.7	132.8	791.9
Tennessee	275.3	343.1	315.3	-8.7	1,218.7
West South Central	1,852.4	2,236.6	2,123.4	172.6	7,072.5
Arkansas	99.7	215.8	128.9	243.0	293.9
Louisiana	180.6	310.0	238.4	89.0	1,868.2
Oklahoma	273.9	291.6	290.1	300.7	544.6
Texas	1,298.2	1,419.4	1,466.0	-440.0	4,365.8
East North Central	1,111.5	620.7	1,445.8	1,439.2	5,327.3
Illinois	-276.1	-375.5	-206.8	-261.2	892.3
Indiana	337.3	-14.3	394.4	194.0	796.7
Michigan	537.3	429.8	812.7	236.5	1,541.9
Ohio	543.1	434.8	632.2	750.4	1,795.5
Wisconsin	-30.1	145.9	13.1	519.5	196.9
West North Central	-185.9	-53.0	-68.7	1,008.1	1,731.8
Iowa	40.7	63.0	47.9	157.3	200.8
Kansas	-34.0	-6.7	-17.9	69.7	269.9
Minnesota	-143.7	-278.2	-125.2	567.4	111.6
Missouri	-36.0	100.4	13.1	-69.7	949.4
Nebraska	-38.9	11.9	-30.8	88.4	85.9
North Dakota	15.7	26.7	23.1	108.9	55.2
South Dakota	10.4	29.8	21.0	76.2	59.1
Mountain	552.2	557.8	633.5	343.3	1,396.7
Arizona	n/a	n/a	n/a	n/a	n/a
Colorado	-6.3	-3.6	15.4	-18.8	307.8
Idaho	44.2	70.1	56.5	67.8	105.0
Montana	49.8	71.7	48.3	98.1	89.2
Nevada	-17.5	-38.9	-10.4	-60.5	131.1
New Mexico	256.7	270.9	274.9	123.1	387.8
Utah	195.8	161.0	215.4	103.1	313.7
Wyoming	29.6	26.6	33.3	30.5	62.2
Pacific	2,109.1	1,390.5	2,402.0	-1,291.3	7,769.8
Alaska	41.6	35.3	44.7	-29.3	153.3
California	1,638.2	835.7	1,889.4	-1,673.7	6,336.6
Hawaii	81.9	84.3	94.5	1.8	205.1
Oregon	235.7	247.9	257.1	217.1	408.6
Washington	111.8	187.3	116.3	192.8	666.3

Note: A negative number indicates a decrease in state expenditures and an increase in federal expenditures.

Table 7B

Static Model Results: Affect of Alternative Swaps on FY 1993 State Finances
(Percentage Change from Current System)

State	% Change in Liability: Swap #10	% Change in Liability: Swap #11	% Change in Liability: Swap #12	% Change in Liability: Swap #13	% Change in Liability: Swap #14 (S.707)
United States	0.5%	2.0%	3.3%	4.0%	52.5%
New England	-33.6%	-30.2%	-32.0%	6.1%	12.3%
Connecticut	-45.9%	-40.3%	-44.2%	16.2%	0.0%
Maine	-15.6%	3.7%	-13.2%	23.3%	49.2%
Massachusetts	-26.5%	-30.6%	-25.1%	-0.5%	9.8%
New Hampshire	-61.1%	-52.3%	-59.5%	-29.6%	41.6%
Rhode Island	-37.8%	-25.4%	-37.1%	20.3%	-5.4%
Vermont	8.1%	31.8%	11.4%	35.4%	43.5%
Middle Atlantic	-32.9%	-26.7%	-31.4%	3.8%	11.5%
New Jersey	-33.7%	-35.5%	-32.1%	-14.6%	20.8%
New York	-40.3%	-29.3%	-39.2%	4.6%	1.1%
Pennsylvania	-4.3%	-9.1%	-1.4%	17.1%	42.0%
South Atlantic	13.4%	14.4%	17.0%	-2.8%	69.9%
Delaware	-17.5%	-13.3%	-14.7%	1.6%	14.3%
District of Columbia	-23.6%	-24.7%	-22.4%	-4.2%	1.9%
Florida	15.0%	16.2%	18.0%	-14.9%	66.6%
Georgia	35.8%	29.9%	41.0%	-4.5%	97.0%
Maryland	-6.9%	15.9%	-4.9%	-16.6%	27.1%
North Carolina	18.1%	23.0%	22.1%	29.3%	88.3%
South Carolina	18.5%	44.8%	26.1%	10.7%	146.6%
Virginia	-7.0%	-0.1%	-3.1%	-10.4%	32.4%
West Virginia	90.8%	131.7%	93.4%	43.1%	178.3%
East South Central	54.1%	68.2%	60.9%	14.9%	150.4%
Alabama	48.7%	76.5%	58.5%	15.2%	169.9%
Kentucky	60.0%	74.5%	66.3%	25.6%	129.4%
Mississippi	141.0%	154.5%	153.1%	43.8%	261.0%
Tennessee	27.2%	33.9%	31.1%	-0.9%	120.3%
West South Central	38.0%	45.9%	43.6%	-3.5%	145.1%
Arkansas	32.1%	69.5%	41.5%	78.3%	94.7%
Louisiana	16.5%	28.3%	21.8%	6.3%	170.4%
Oklahoma	60.7%	64.7%	64.3%	66.7%	120.8%
Texas	43.1%	47.1%	48.6%	-14.6%	144.8%
East North Central	10.3%	5.7%	13.4%	13.3%	49.3%
Illinois	9.7%	-11.9%	-6.6%	-8.3%	28.3%
Indiana	28.4%	-1.2%	33.3%	16.4%	67.4%
Michigan	19.9%	15.9%	22.7%	8.8%	60.8%
Ohio	20.4%	16.3%	23.7%	28.1%	67.3%
Wisconsin	-2.7%	13.3%	1.2%	47.2%	18.1%
West North Central	-5.0%	-1.4%	-1.8%	27.0%	46.4%
Iowa	8.8%	13.6%	10.3%	36.0%	43.3%
Kansas	-7.3%	-1.4%	-3.8%	15.0%	58.0%
Minnesota	-11.4%	-22.0%	-9.9%	44.9%	8.8%
Missouri	-3.3%	9.3%	1.2%	-6.4%	87.9%
Nebraska	-14.6%	4.5%	-11.5%	33.2%	32.0%
North Dakota	17.1%	29.1%	25.1%	118.5%	60.1%
South Dakota	10.9%	31.3%	22.0%	79.9%	62.0%
Mountain	36.4%	36.7%	41.7%	22.6%	92.0%
Arizona	n/a	n/a	n/a	n/a	n/a
Colorado	-1.0%	-0.6%	2.5%	-3.1%	50.2%
Idaho	40.6%	64.5%	51.9%	62.4%	96.6%
Montana	40.4%	58.1%	39.2%	79.5%	72.0%
Nevada	-7.2%	-16.1%	-4.3%	-25.0%	54.1%
New Mexico	125.2%	132.1%	134.1%	60.0%	189.1%
Utah	118.8%	97.7%	130.7%	62.6%	190.4%
Wyoming	48.9%	43.9%	54.9%	50.4%	102.7%
Pacific	16.1%	10.6%	18.4%	-9.9%	59.4%
Alaska	19.5%	16.6%	21.0%	-15.8%	72.1%
California	15.4%	7.9%	17.8%	0.6%	59.6%
Hawaii	28.2%	29.0%	32.5%	0.6%	70.6%
Oregon	46.4%	48.8%	50.6%	42.8%	80.5%
Washington	7.7%	12.9%	8.0%	13.3%	46.0%

Note: A negative percentage indicates a decrease in state expenditures and an increase in federal expenditures.

8/11/95 16:16

only \$1.4 billion, or 2 percent. If Medicaid grows faster than the cash programs and food stamps, states would be winners in aggregate over time. New York and New Jersey win and Texas is a loser in the short run. While the variations across other states seem to be relatively low in dollar terms, there are some exceptions. Mississippi, New Mexico and West Virginia each lose by over 100 percentage points.

Swap 12 is a small variation on swap 10, in which WIC goes to the states and long term care for adults becomes a federal responsibility. On aggregate these differences create state losses of an additional \$2 billion. Impacts for individual states and across the regions look quite similar to swap 10.

Swap 13 takes an opposite tack and moves long term care to the states and retains the rest of Medicaid at the federal level. This allocation has some intuitive appeal because long term care is one of the least uniform benefits in the Medicaid program. There is currently an enormous amount of variation in long term care spending by state, with states and localities differing substantially in their preferred approaches to providing this benefit. Food stamps and WIC are also kept as federal programs under this alternative. In this case aggregate state losses are \$2.8 billion. The biggest losing state in terms of absolute dollars is Ohio, followed by Minnesota, New York, Pennsylvania and Wisconsin. These losses are, however, considerably lower than the highest losses by other options. Moreover, if one criterion is to minimize losses by states or regions, this is an appealing option. The largest percentage loser among regions is West North Central. The only swap option that does better than this in minimizing regional losses is the original Kassebaum proposal, but largely because it created so few losers. Winning states are all below \$500 million with the exception of California, which has a decrease in

burden of \$1.7 billion. On a percentage basis, only the Pacific and South Atlantic regions are winners, and the largest winner among the states is New Hampshire with a 29.6 percent reduction in burden.

The final option shown here is the second Kassebaum proposal (S.707). It creates major state losses by shifting everything except long term care and acute care for the aged and disabled to the states. Again, this is a straightforward proposal and makes considerable logical sense. It does not, however, operate as a "swap" in terms of evening out burdens. Ten states would lose in excess of a billion dollars under this proposal and only one state (Rhode Island) gains. On a percentage basis, the East South Central is a substantial loser and Mississippi leads all the states in percentage losses.

There are a few consistent trends in these swaps. Three regions -- East South Central, West South Central, and Mountain -- lose from every option and Pacific loses in all cases except swap 13. Moreover, all states in the two South Central regions lose in every option except swap 13, in which only Tennessee and Texas gain. No region or state is a consistent winner across all the swap proposals, however, likely because few of the swaps advantage the states in aggregate.

Case 2. Potential Behavioral Responses

Unfortunately, as described above, the economic literature is of only limited help in predicting the responses of state governments following major changes in the division of program responsibilities such as those suggested by various swap proposals. Actual experiences with financing changes have occurred with a small number of programs, and those changes have largely been quite small relative to the substantial redistributions being proposed in swaps. Thus, previous estimates of elasticities may not be as helpful in predicting change as if more marginal

adjustments were under consideration. Interactions between the multiple simultaneous changes can also cause significant and difficult-to-predict effects. In addition, as noted previously, financial incentives would not be the only driving force behind state government driven policy changes. Political considerations may play an even larger role in determining state responses. Consequently, substantial uncertainty surrounds the predictions of the net effects of swap proposals on state spending.

The examples presented here are meant to be illustrative only. To estimate states' responses to a swap proposal, we use ranges of behavioral responses found in the literature. Confidence in any particular figure should not be high, though we hope that the ranges will be somewhat reflective of the potential effects of a swap plan. In order to simplify the discussion and minimize interactive effects, we provide an example of a Medicaid-only swap.

The Medicaid-only swap example uses the policies included in the Medicaid portion of the current Kassebaum swap (S. 707). The federal government assumes responsibility for long term care and acute care for the elderly and disabled, while the states receive responsibility for the remainder of the Medicaid program, including DSH. Table 8 shows the static results (comparable to earlier tables), if the federal and state governments kept post-swap spending for each component of the Medicaid program at its current levels. Obviously, such a scenario is unlikely to hold since states will undoubtedly respond to the changed incentives. There are two economic phenomena that are likely to affect states' decisions about Medicaid spending following a swap: a price effect and an income effect.²¹ These incentive effects are explained below.

²¹The price effect itself is, in turn, composed of two distinct phenomenon: a substitution effect and an income effect. These separate effects are explained in detail in Appendix A.

Table 8
Static Model Results for the Medicaid-Only Swap
(dollars in millions)

	Federal Government Receives Responsibility For:				State Governments Receive Responsibility For:					
	Long Term Care	Acute Care for Elderly & Disabled	Federal Share of Admin Costs	Federal Total	DSH	Medicaid Payments to HMOs	Kids Acute Care	Adults Acute Care	State Admin Share	Total State
United States	44,177.9	31,004.0	2,811.2	77,993.0	16,944.0	3,939.5	15,770.9	1,331.4	1,906.9	51,878.1
New England	3,853.3	1,918.7	181.9	5,941.8	1,564.8	324.5	739.7	611.8	88.1	3,328.9
Connecticut	1,165.6	368.5	41.1	1,575.2	417.3	0.0	182.3	144.1	19.9	783.7
Maine	242.7	178.7	16.1	567.7	164.1	0.0	72.9	66.3	10.1	319.4
Massachusetts	1,810.7	978.7	67.9	2,855.2	484.5	309.7	372.5	290.0	39.2	1,494.6
New Hampshire	227.7	69.8	8.2	303.7	362.9	8.2	39.9	34.6	9.8	475.2
Rhode Island	404.5	230.5	14.6	649.6	97.2	1.6	47.7	47.5	4.4	106.4
Vermont	112.1	71.1	14.3	197.5	19.6	0.0	24.5	29.3	5.7	78.0
Middle Atlantic	13,006.4	6,620.8	812.2	20,239.4	4,458.1	720.3	2,981.9	2,159.6	322.9	16,643.4
New Jersey	1,842.5	1,057.9	80.3	2,780.7	1,088.2	311.5	307.3	1,114.4	59.7	2,065.3
New York	8,629.8	4,574.8	398.9	13,803.0	2,558.7	256.7	2,099.7	1,308.9	185.2	8,409.1
Pennsylvania	2,534.2	988.3	133.1	3,655.7	811.1	432.2	514.3	332.5	78.9	2,169.1
South Atlantic	5,868.0	5,131.8	400.5	11,200.1	1,709.8	541.9	3,003.7	2,172.9	273.5	7,892.6
Delaware	109.3	72.5	10.7	192.9	5.2	0.0	39.2	25.8	3.9	74.1
District of Columbia	261.4	198.9	15.0	475.8	48.1	25.0	98.7	56.9	7.6	221.1
Florida	1,376.5	1,518.7	88.9	2,984.0	239.7	369.3	1,072.5	374.4	63.1	2,110.0
Georgia	749.4	793.9	60.1	1,602.2	309.4	0.0	419.5	527.6	48.9	1,305.4
Maryland	604.8	625.8	61.5	1,292.1	171.9	141.7	304.6	205.7	36.5	796.3
North Carolina	1,092.8	818.5	51.9	1,763.9	345.5	5.9	431.6	402.2	40.1	1,225.4
South Carolina	464.1	393.9	37.7	895.6	440.7	0.1	215.8	189.1	36.3	860.7
Virginia	682.4	518.8	50.3	1,251.3	130.9	0.0	249.9	210.2	24.7	615.5
West Virginia	328.5	382.2	18.8	730.3	100.3	0.0	112.3	202.1	12.4	492.1
East South Central	2,961.4	2,187.0	117.5	4,365.9	1,136.7	31.4	1,055.9	899.5	96.5	3,210.9
Alabama	482.2	387.4	19.9	889.4	419.1	0.5	177.7	160.3	17.1	774.9
Kentucky	537.8	639.8	32.9	1,210.3	137.0	0.0	295.9	293.4	16.1	705.4
Mississippi	314.8	407.0	18.1	740.0	152.2	0.0	186.9	155.3	11.9	466.4
Tennessee	718.8	752.9	46.7	1,518.2	430.2	30.8	440.3	299.5	39.3	1,244.2
West South Central	3,704.9	2,905.9	247.9	6,858.6	2,756.7	0.0	2,029.0	1,573.4	224.2	6,563.2
Arkansas	456.0	331.3	28.3	815.6	2.5	0.0	158.9	152.5	8.7	250.9
Louisiana	927.9	884.6	31.1	1,943.5	1,217.8	0.0	384.7	315.6	34.9	1,950.9
Oklahoma	411.9	226.3	54.3	712.5	27.4	0.0	212.2	135.9	29.3	400.9
Texas	1,827.0	1,463.8	131.8	3,422.6	1,513.0	0.0	1,275.2	1,039.5	153.2	3,881.0
East North Central	7,581.8	4,884.3	482.9	12,938.7	1,275.2	1,226.4	2,482.6	2,013.7	256.2	7,234.0
Illinois	1,908.4	1,473.5	172.0	3,453.9	240.1	119.0	964.3	536.1	89.0	1,788.8
Indiana	1,081.9	564.5	29.3	1,672.7	33.8	440.6	364.2	330.6	19.7	1,187.9
Michigan	1,460.5	1,104.0	108.2	2,672.7	307.4	442.7	503.3	375.9	1,974.0	5,895.9
Ohio	2,175.9	1,135.7	104.2	3,415.7	448.0	201.1	878.8	534.8	54.9	1,826.5
Wisconsin	1,065.0	608.6	52.2	1,723.7	7.8	158.4	172.6	104.4	13.9	457.2
West North Central	3,300.1	1,523.2	202.5	5,025.8	827.1	211.1	812.1	822.0	97.5	2,869.9
Iowa	423.9	289.9	28.9	742.7	1.1	1.8	143.0	124.7	11.1	284.5
Kansas	354.9	154.9	18.4	521.4	184.4	0.1	43.1	68.8	13.8	300.3
Minnesota	1,301.4	300.7	88.0	1,690.0	32.3	183.1	102.1	157.5	31.0	586.0
Missouri	658.3	510.7	37.7	1,201.8	703.1	26.1	207.7	145.9	30.3	1,112.9
Nebraska	261.0	147.3	16.1	420.5	3.3	0.1	108.2	44.2	6.9	162.7
North Dakota	198.0	51.0	10.2	259.2	0.0	0.0	30.7	29.4	2.8	61.9
South Dakota	137.0	69.8	8.2	212.8	0.0	0.0	37.0	22.7	1.9	61.5
Mountain	1,180.2	957.1	87.9	2,131.2	225.7	59.3	508.0	478.5	54.1	1,326.5
Arizona	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Colorado	384.7	277.1	18.2	680.0	130.5	17.4	154.0	128.0	11.9	441.7
Idaho	129.6	81.2	15.8	223.3	1.0	0.1	44.2	40.7	8.4	92.4
Montana	153.1	97.7	10.1	260.9	0.5	0.2	38.7	33.0	2.8	73.4
Nevada	121.1	100.4	7.8	229.4	60.3	13.2	56.4	52.1	7.2	209.1
New Mexico	188.0	174.2	15.2	377.4	8.8	0.0	96.5	106.8	8.9	217.9
Utah	157.2	97.8	10.0	270.0	4.5	18.5	88.0	101.9	14.0	236.8
Wyoming	55.5	29.0	5.0	89.6	0.1	0.0	27.2	22.9	3.0	53.2
Pacific	3,796.0	4,977.4	518.1	9,291.5	2,897.4	824.8	2,179.3	2,785.9	502.9	8,199.0
Alaska	56.7	49.3	7.8	113.9	33.3	0.0	67.7	91.7	12.1	174.8
California	2,296.4	4,096.4	358.4	6,750.4	2,542.5	712.1	1,688.8	2,222.9	400.6	7,546.7
Hawaii	122.9	97.5	9.9	230.3	43.9	0.0	81.9	48.5	7.2	161.4
Oregon	430.7	182.8	55.4	678.7	20.8	64.3	118.5	128.9	26.8	361.9
Washington	890.1	541.6	86.5	1,518.2	257.0	42.4	291.6	323.8	53.5	938.2

Source of Medicaid data: Urban Institute adjustments to Health Care Financing Administration Medicaid 64 & 2082 data

- The Price Effect:** "Prices" of programs fully assumed by states will rise dramatically from as little as 20 percent of costs to 100 percent of costs. Under current Medicaid law, the federal government pays a percentage of a state's expenditures on the Medicaid program, with that percentage varying inversely with the state's per capita personal income. The federal share ranges from 50 percent to 83 percent. So, effectively, the state's price is only a fraction of the costs it incurs, with that fraction ranging from 17 percent to 50 percent, depending upon the state's per capita personal income. Under a swap, those parts of the Medicaid program which are devolved to state responsibility will no longer be contributed to by the federal government; consequently, any costs incurred by the state must be wholly financed by the state. Since health care is a normal good (i.e., as price falls, consumption of the good increases and as price increases, consumption of the good falls), we can expect that a state will choose to consume fewer health care services as the relative price it faces climbs.
- The Income Effect:** Where the federal government takes over programs, states effectively receive a boost in their "incomes." The income effect is the result of the federalization of long term care and acute care services for the elderly and disabled. As states are relieved of this responsibility, the elimination of the state financial burden of providing these services can be expected to be treated in much the same way as an increase in state government income. As was mentioned previously, such an increase in income is, in general, devoted in some part to new public spending and in some part to reducing private tax burdens for state residents.

Table 9 illustrates a range of magnitudes of possible price effects. Orr's²² work provides a price elasticity of demand for public program spending at the low end of the literature, while Gramlich's²³ work provides one at the high end. The price responses calculated purely off of these elasticities only reflect the differences in the relative price increases across states. These estimates do not incorporate the preference variation across states beyond what is evidenced by the current levels of spending. Given that there is no justifiable mechanism for adjusting the elasticities to take potential variations in preferences into account, we use these two estimated elasticities to bound the possible price responses.

²²Orr, op. cit., 1976.

²³Gramlich, op. cit. 1982.

Table 9

Percentage Change in Expenditures on Acute Care for the Non-Elderly As a Result of Effective Price Increase Facing State if Full Responsibility for Financing These Services is Devolved to the States

(Ranges are Based Upon Estimated Elasticities Found in the Literature)

(\$ in millions)

	Current Effective Price (1-FMAP)	Percentage Increase in Price from (1-FMAP)/cost to cost (*)	Current Spending Per Low Income (in dollars) (**)	Low End of Range: % Change in Benefits (***)	High End of Range: % Change in Benefits (****)
New England					
Connecticut	0.5000	66.7%	795.9	-15.3%	-48.5%
Maine	0.3819	89.5%	502.3	-20.6%	-60.2%
Massachusetts	0.5000	66.7%	927.9	-15.3%	-48.5%
New Hampshire	0.5000	66.7%	460.5	-15.3%	-48.5%
Rhode Island	0.4636	73.3%	560.2	-16.9%	-52.1%
Vermont	0.4012	85.5%	517.2	-19.7%	-58.3%
Middle Atlantic					
New Jersey	0.5000	66.7%	722.0	-15.3%	-48.5%
New York	0.5000	66.7%	854.5	-15.3%	-48.5%
Pennsylvania	0.4452	76.8%	537.8	-17.7%	-53.9%
South Atlantic					
Delaware	0.5000	66.7%	524.8	-15.3%	-48.5%
District of Columbia	0.5000	66.7%	1,018.8	-15.3%	-48.5%
Florida	0.4497	75.9%	541.4	-17.5%	-53.5%
Georgia	0.3792	90.0%	538.3	-20.7%	-60.5%
Maryland	0.5000	66.7%	751.5	-15.3%	-48.5%
North Carolina	0.3408	98.3%	558.5	-22.6%	-64.3%
South Carolina	0.2872	110.8%	383.5	-25.5%	-69.7%
Virginia	0.5000	66.7%	373.5	-15.3%	-48.5%
West Virginia	0.2371	123.3%	675.2	-28.4%	-74.8%
East South Central					
Alabama	0.2855	111.2%	279.9	-25.6%	-69.9%
Kentucky	0.2831	111.7%	540.5	-25.7%	-70.2%
Mississippi	0.2099	130.6%	326.9	-30.0%	-77.6%
Tennessee	0.3243	102.0%	558.0	-23.5%	-66.0%
West South Central					
Arkansas	0.2559	118.5%	352.1	-27.3%	-72.9%
Louisiana	0.2629	116.7%	519.0	-26.8%	-72.2%
Oklahoma	0.3033	106.9%	408.9	-24.8%	-68.1%
Texas	0.3556	95.1%	476.7	-21.9%	-62.8%
East North Central					
Illinois	0.5000	66.7%	533.9	-15.3%	-48.5%
Indiana	0.3679	92.4%	951.5	-21.3%	-61.6%
Michigan	0.4416	77.5%	579.4	-17.8%	-54.3%
Ohio	0.3975	86.2%	615.4	-19.8%	-56.6%
Wisconsin	0.3958	86.6%	482.9	-19.9%	-56.8%
West North Central					
Iowa	0.3726	91.4%	506.5	-21.0%	-61.1%
Kansas	0.4182	82.0%	393.8	-18.9%	-56.6%
Minnesota	0.4507	75.7%	622.2	-17.4%	-53.4%
Missouri	0.3974	86.2%	304.4	-19.6%	-58.7%
Nebraska	0.3868	88.4%	534.1	-20.3%	-59.7%
North Dakota	0.2779	113.0%	478.2	-26.0%	-70.6%
South Dakota	0.2973	108.3%	362.3	-24.9%	-66.7%
Mountain					
Arizona	n.e.	n.e.	n.e.	n.e.	n.e.
Colorado	0.4558	74.8%	460.2	-17.2%	-52.8%
Idaho	0.2680	110.6%	326.6	-25.4%	-69.6%
Montana	0.2908	109.8%	336.7	-25.3%	-69.3%
Nevada	0.4772	70.8%	448.9	-16.3%	-50.7%
New Mexico	0.2615	117.1%	411.7	-26.9%	-72.8%
Utah	0.2471	120.7%	576.8	-27.8%	-73.8%
Wyoming	0.3289	101.0%	553.9	-23.2%	-65.5%
Pacific					
Alaska	0.5000	66.7%	1,049.9	-15.3%	-48.5%
California	0.5000	66.7%	548.3	-15.3%	-48.5%
Hawaii	0.5000	66.7%	549.7	-15.3%	-48.5%
Oregon	0.3761	90.7%	508.2	-20.9%	-60.8%
Washington	0.4498	75.9%	735.2	-17.5%	-53.4%

* Calculated as (1-current state share) divided by the average of current state share and 1.0.

** Total current Medicaid spending (state + federal) for acute care for the non-elderly in each state divided by the number of non-elderly in the state below 150% of poverty.

*** Equal to (percentage change in price) / (-.23). -.23 is the Orr (1976) estimated price elasticity.

**** Equal to (percentage change in price) / elasticity. Elasticity is equal to the price elasticity for each state implied by Gramlich (1982). Calculation of these elasticities is shown in the appendix table.

8/8/95 14.24

Table 9 shows the post-swap estimated percentage reductions in total spending (state plus federal) on acute care for the non-elderly. The low end percentage reduction in spending was calculated as follows: % reduction = (% price Δ) * ϵ_{ORR} , where ϵ_{ORR} is the elasticity calculated by Orr (-.23), and “% price Δ ” is the relative increase in price when the state share moves from its current system level to zero. Likewise, the high end percentage reduction in spending was calculated as follows: % reduction = (% price Δ) * ϵ_{GRAM} , where ϵ_{GRAM} is the appropriate elasticity for each state as calculated by Gramlich.²⁴ The table also shows the current level of state spending on these services per low income non-elderly person in the state in order to provide an indicator of relative levels of current state program generosity.

As can be seen in the table, the range of estimates is quite large. States such as Mississippi and Arkansas with high current matching rates have the largest assumed price responses. Mississippi is estimated to have a 30 percent reduction in spending under the low end assumptions and a 78 percent reduction under the high end; the range for Arkansas is 27 percent to 73 percent. Many of these high matching rate states also have low relative program generosity. States such as the District of Columbia, Illinois, New York, and California which have low matching rates are expected to have the most modest price responses, a 15 to 49 percent reduction in program spending. The lower the current matching rate, the smaller is the relative price increase when the federal matching rate is eliminated. Southern states tend to have higher current matching rates, and consequently will tend to have larger reductions in program spending, all else being equal. The higher income New England and Pacific states will tend to experience smaller reductions

²⁴Details of the calculation of Gramlich's implied elasticities are in Appendix B to this report.

relative to current system spending.

Table 10 illustrates a range of possible income effects resulting from the federalization of acute care for the elderly and disabled and long term care. As was discussed in the previous section, the economic literature suggests that anywhere from 25 percent to 100 percent of new state income is devoted to public spending. The 25 percent assumption is shown in Table 10's low end of range estimates and the 100 percent assumption is reflected in the high end of range estimates. These calculations are based upon the state savings from the partial Medicaid federalization. As can be seen in the table, those states with the largest current spending on long term care and elderly/disabled programs, such as New York and California, are likely to see the largest income effects. It is important to keep in mind, however, the size of these programs relative to the full size of the states' current Medicaid program. Particularly in the case of California, large absolute dollars on long term care do not necessarily translate into generous long term care programs, given the population size involved. The largest relative income effects would likely be seen in Rhode Island and Delaware, where state savings would amount to 34-35 percent of total current Medicaid spending. Connecticut, New York, the District of Columbia, and Virginia are other states that would experience large income effects relative to current spending levels. States in the southern regions are likely to have the lowest relative income effects, whereas the New England states, as a group, will tend to have the highest.

Table 11 presents a hypothetical reallocation of Medicaid dollars following the federalization of long term care and acute care for the elderly and disabled. We assume that total dollars for these services remains constant, but that the federal program would reallocate the dollars to be spent in each state according to the share of the low income (under 150% of

Table 10

**Potential State Income Effect Resulting from the Federalization of Medicaid
Long Term Care and Acute Care for the Elderly and Disabled
(\$ in millions)**

	State Savings from Federalization of LTC and Acute Care for the Elderly & Disabled	State Savings from Federalization as Percentage of Total Current Medicaid Spending	Low End of Range Savings Devoted to Public Spending	High End of Range Savings Devoted to Public Spending
New England				
Connecticut	767.1	32.8%	191.8	767.1
Maine	207.3	23.6%	51.8	207.3
Massachusetts	1,293.7	31.2%	323.4	1,293.7
New Hampshire	148.7	19.1%	37.2	148.7
Rhode Island	294.4	34.7%	73.8	294.4
Vermont	73.5	26.7%	18.4	73.5
Middle Atlantic				
New Jersey	1,350.2	27.9%	337.6	1,350.2
New York	6,702.1	33.2%	1,675.5	6,702.1
Pennsylvania	1,568.3	26.9%	392.1	1,568.3
South Atlantic				
Delaware	91.4	34.2%	22.9	91.4
District of Columbia	230.1	32.4%	57.5	230.1
Florida	1,301.0	25.5%	325.3	1,301.0
Georgia	584.8	20.1%	146.2	584.8
Maryland	615.3	29.8%	153.8	615.3
North Carolina	583.1	19.5%	145.8	583.1
South Carolina	246.4	14.0%	61.6	246.4
Virginia	600.5	32.2%	150.1	600.5
West Virginia	170.9	13.9%	42.7	170.9
East South Central				
Alabama	251.1	15.0%	62.8	251.1
Kentucky	333.3	17.4%	83.3	333.3
Mississippi	151.5	12.4%	37.9	151.5
Tennessee	476.6	17.3%	119.1	476.6
West South Central				
Arkansas	202.0	18.9%	50.5	202.0
Louisiana	476.5	12.6%	119.1	476.5
Oklahoma	217.8	18.5%	54.5	217.8
Texas	1,170.2	15.8%	292.6	1,170.2
East North Central				
Illinois	1,641.0	31.3%	410.2	1,641.0
Indiana	605.7	21.2%	151.4	605.7
Michigan	1,132.5	24.9%	283.1	1,132.5
Ohio	1,316.3	24.6%	329.1	1,316.3
Wisconsin	661.6	30.3%	165.4	661.6
West North Central				
Iowa	265.9	25.9%	66.5	265.9
Kansas	214.5	23.3%	53.6	214.5
Minnesota	722.0	31.6%	180.5	722.0
Missouri	464.6	20.1%	116.1	464.6
Nebraska	158.0	26.8%	39.5	158.0
North Dakota	58.5	20.7%	14.6	58.5
South Dakota	61.4	22.4%	15.4	61.4
Mountain				
Arizona	n.a.	n.a.	n.a.	n.a.
Colorado	301.6	26.9%	75.4	301.6
Idaho	59.8	19.0%	15.0	59.8
Montana	72.9	21.7%	18.2	72.9
Nevada	105.7	24.1%	26.4	105.7
New Mexico	94.7	15.9%	23.7	94.7
Utah	63.0	12.4%	15.7	63.0
Wyoming	27.8	19.5%	7.0	27.8
Pacific				
Alaska	53.0	18.4%	13.2	53.0
California	3,196.0	22.4%	799.0	3,196.0
Hawaii	110.2	27.7%	27.6	110.2
Oregon	234.4	22.5%	58.6	234.4
Washington	644.0	26.2%	161.0	644.0

Notes

* Range of income effect is based upon evidence from the literature that anywhere from 25 to 100% of an increase in public sector income will be used for public sector spending, the rest being used to lower private sector tax burdens.

* The denominator for column 2 is equal to the sum of column 1 of Table 1-A and column 1 of Table 1-B

10/2/95 14 37

poverty) elderly residing in that state. In other words, post-swap spending in a state is equal to that state's share of total national low income elderly persons multiplied times the current total national spending on long term care and acute care for the elderly and disabled, approximately \$75 billion. The percentage change in spending on these services in each state is shown in the last column of Table 11. Alabama would be the greatest relative winner in such a revamping, with Florida and Mississippi being other big winners. The Southern and South Atlantic regions tend to be winners. Connecticut, the District of Columbia, and New York would see the largest relative losses under such a scenario. The New England states overall tend to lose. These states currently have generous long term care programs relative to their share of the nation's low income elderly population.

Tables 12 and 13 attempt to integrate these various changes into a net effect on spending within each state.²⁵ Table 12 contains estimates using the most optimistic assumptions -- those leading to the smallest changes in state spending post swap. In other words, the smallest estimated price responses (from eliminating the federal match on some services) and the largest estimated income responses (from federalization of the other services) are used in Table 12. Table 13 contains estimates using the most pessimistic assumptions (those generating the largest reductions in state spending): the largest price responses and the smallest income responses.

A number of assumptions go into our calculation of the net effect of the changes explained above. These assumptions are detailed as follows:

²⁵DSH spending is not included in these tables. Given that state DSH dollars are raised in a variety of ways across states, and since the DSH dollars in a number of those states do not appear to represent new state spending (see Ku and Coughlin, op. cit.), there seemed to be no basis on which to judge state's response to a devolution of responsibility for DSH spending.

Table 11

**Spending on Long Term Care and Acute Care for the Elderly & Disabled, by State
Before and After Hypothetical Implementation of Swap**

	State Share of Low Income Elderly	Current Total Spending on LTC & Acute for Elderly & Disabled	Hypothetical (post swap) Federal Spending on LTC & Acute Care for Elderly & Disabled (*)	Percentage change in Spending in State, Post-Swap
New England				
Connecticut	0.8%	1,534.1	584.1	-61.9%
Maine	0.4%	542.8	310.6	-42.8%
Massachusetts	2.5%	2,587.4	1,844.2	-28.7%
New Hampshire	0.4%	297.5	265.6	-10.7%
Rhode Island	0.5%	635.0	351.3	-44.7%
Vermont	0.2%	183.1	162.4	-11.3%
Middle Atlantic				
New Jersey	3.1%	2,700.4	2,344.7	-13.2%
New York	7.9%	13,404.2	5,944.0	-55.7%
Pennsylvania	5.8%	3,522.6	4,387.5	24.6%
South Atlantic				
Delaware	0.2%	182.8	138.0	-24.5%
District of Columbia	0.2%	460.2	176.8	-61.6%
Florida	7.1%	2,893.1	5,347.7	84.8%
Georgia	3.2%	1,542.2	2,381.7	54.4%
Maryland	1.4%	1,230.6	1,064.3	-11.9%
North Carolina	3.5%	1,711.1	2,644.3	54.5%
South Carolina	1.8%	857.9	1,212.3	41.3%
Virginia	2.1%	1,201.0	1,561.0	30.0%
West Virginia	1.0%	720.7	753.5	4.5%
East South Central				
Alabama	2.3%	879.6	1,703.0	93.6%
Kentucky	2.1%	1,177.4	1,585.8	34.7%
Mississippi	1.8%	721.9	1,207.3	67.2%
Tennessee	2.5%	1,469.5	1,888.5	28.5%
West South Central				
Arkansas	1.5%	789.3	1,093.2	38.5%
Louisiana	2.1%	1,812.4	1,565.2	-13.6%
Oklahoma	1.4%	718.2	1,046.2	45.7%
Texas	6.7%	3,290.8	5,060.0	53.8%
East North Central				
Illinois	4.5%	3,281.9	3,345.9	1.9%
Indiana	2.4%	1,646.4	1,805.0	9.6%
Michigan	3.0%	2,564.5	2,229.1	-13.1%
Ohio	4.1%	3,311.4	3,076.1	-7.1%
Wisconsin	1.8%	1,671.6	1,368.7	-18.1%
West North Central				
Iowa	1.1%	713.7	853.6	19.6%
Kansas	0.8%	512.9	597.6	16.5%
Minnesota	1.5%	1,602.0	1,152.5	-28.1%
Missouri	2.1%	1,169.1	1,562.2	33.6%
Nebraska	0.6%	408.4	469.2	14.9%
North Dakota	0.2%	210.6	181.8	-13.7%
South Dakota	0.3%	206.6	258.1	24.9%
Mountain				
Arizona	n/a	n/a	n/a	n/a
Colorado	0.9%	861.8	641.2	-23.1%
Idaho	0.4%	207.7	279.8	34.7%
Montana	0.3%	250.8	207.1	-17.4%
Nevada	0.4%	221.5	318.6	43.8%
New Mexico	0.6%	362.2	445.8	23.1%
Utah	0.4%	254.8	270.1	6.0%
Wyoming	0.1%	84.5	90.8	7.4%
Pacific				
Alaska	0.1%	106.0	65.4	-38.3%
California	9.6%	6,392.0	7,249.7	13.4%
Hawaii	0.4%	220.4	334.9	51.9%
Oregon	1.1%	623.3	848.2	36.1%
Washington	1.2%	1,431.7	886.9	-38.1%
Total	100.0%	75,181.7	75,181.7	0.0%

* Note: Post-swap dollars allocated according to states' share of low income elderly. Post-swap dollars are equal to (total current spending) * (state share of low income elderly). Both the shares of low income elderly and the current total spending figures are rounded in the table. Consequently, multiplication using figures in columns 1 & 2 may not lead to precisely the same numbers contained in column 3 of the table.

10/2/95 14:37

Table 12
Effect of Hypothetical Combination of Price and Income Effects on Spending in Each State
Most Optimistic Scenario: Larger Assumed Income Effect, Smaller Assumed Price Effect
(\$ in millions)

State	(A) Change in Spending in State on Acute Care for Non-Elderly Due to Pure Price Effect (*)	(B) State Savings Due to Federalization of LTC/elderly/disabled to be Devoted to State Public Spending (**)	(C) Change in Spending on LTC/elderly/disabled in State After Applying State Savings, If Applicable (***)	(D) Change in Acute Care Spending on Non-Elderly After Applying State Savings If Applicable (****)	(E) Percentage Change in Total Medicaid Benefit Spending Taking All Effects Into Account
New England					
Connecticut	-50.1	767.1	-163.0	-50.1	-12.5%
Maine	-29.7	207.3	-24.9	0.0	-7.5%
Massachusetts	-149.1	1,293.7	0.0	0.0	0.0%
New Hampshire	-12.7	148.7	0.0	0.0	0.0%
Rhode Island	-16.3	294.4	0.0	-5.6	-0.6%
Vermont	-10.6	73.5	0.0	0.0	0.0%
Middle Atlantic					
New Jersey	-140.7	1,350.2	0.0	0.0	0.0%
New York	-562.0	6,702.1	-758.1	-562.0	-7.7%
Pennsylvania	-225.9	1,568.3	864.9	0.0	16.0%
South Atlantic					
Delaware	-10.0	91.4	0.0	0.0	0.0%
District of Columbia	-27.7	230.1	-53.3	-27.7	-12.6%
Florida	-317.1	1,301.0	2,454.6	0.0	52.1%
Georgia	-196.1	584.6	839.6	0.0	33.7%
Maryland	-100.0	615.3	0.0	0.0	0.0%
North Carolina	-189.9	583.1	933.2	0.0	36.6%
South Carolina	-97.5	246.4	354.4	0.0	26.8%
Virginia	-70.5	600.5	360.0	0.0	21.7%
West Virginia	-106.2	170.9	32.6	0.0	3.0%
East South Central					
Alabama	-66.6	251.1	623.5	0.0	67.6%
Kentucky	-141.2	333.3	406.4	0.0	23.7%
Mississippi	-96.6	151.5	485.3	0.0	46.5%
Tennessee	-162.1	476.6	419.1	0.0	18.7%
West South Central					
Arkansas	-65.2	202.0	303.9	0.0	29.5%
Louisiana	-188.0	476.5	0.0	0.0	0.0%
Oklahoma	-85.6	217.8	328.0	0.0	30.8%
Texas	-506.1	1,170.2	1,769.2	0.0	31.6%
East North Central					
Illinois	-223.6	1,841.0	63.9	0.0	1.3%
Indiana	-241.3	605.7	156.6	0.0	5.7%
Michigan	-223.3	1,132.5	0.0	0.0	0.0%
Ohio	-261.3	1,316.3	0.0	0.0	0.0%
Wisconsin	-86.8	661.6	0.0	0.0	0.0%
West North Central					
Iowa	-56.7	265.9	139.6	0.0	14.2%
Kansas	-36.3	214.5	84.5	0.0	12.0%
Minnesota	-92.8	722.0	0.0	0.0	0.0%
Missouri	-75.3	464.6	393.2	0.0	25.4%
Nebraska	-31.0	158.0	60.6	0.0	10.6%
North Dakota	-15.4	58.5	0.0	0.0	0.0%
South Dakota	-14.9	61.4	51.5	0.0	19.3%
Mountain					
Arizona	n.a.	n.a.	n.a.	n.a.	n.a.
Colorado	-51.5	301.6	0.0	0.0	0.0%
Idaho	-21.6	59.6	72.1	0.0	24.6%
Montana	-16.2	72.9	0.0	0.0	0.0%
Nevada	-19.8	105.7	97.1	0.0	26.3%
New Mexico	-53.9	94.7	63.6	0.0	14.9%
Utah	-60.6	63.0	15.3	0.0	3.2%
Wyoming	-11.7	27.8	5.3	0.0	4.6%
Pacific					
Alaska	-19.6	53.0	0.0	-7.4	-3.1%
California	-705.9	3,196.0	857.7	0.0	7.6%
Hawaii	-17.8	110.2	114.5	0.0	34.0%
Oregon	-65.0	234.4	224.9	0.0	24.1%
Washington	-109.8	644.0	0.0	-10.4	-0.5%

* Low and price elasticity estimate (from Table 9) multiplied by current system acute care spending for the non-elderly (from Table 6 Total State less DSH less State Share of Administrative Costs)

** High end of range estimate from Table 10

*** If Table 11, last column, shows a decrease in post-swap spending on long term care and acute care for the elderly and disabled in a state, then savings from column B Table 12 are applied to move these categories of spending back toward the status quo. If the last column of Table 11 shows a post-swap increase in spending, no savings from column B are applied here.

**** If there are state savings from column B in excess of those applied in column C, those savings are applied to increasing estimated spending on acute care for the non-elderly toward the level of the status quo.

***** Any state savings from column B in excess of those applied in columns C or D are assumed to be used for other (non-Medicaid) public spending or for decreasing the state's private tax burden.

8/6/95 14.34

Table 13
Effect of Hypothetical Combination of Price and Income Effects on Spending in Each State
Most Pessimistic Scenario: Smaller Assumed Income Effect, Larger Assumed Price Effect
 (\$ in millions)

State	(A) Change in Spending in State on Acute Care for Non-Elderly Due to Pure Price Effect (*)	(B) State Savings Due to Federalization of LTC/Elderly/Disabled to be Devoted to State Public Spending (**)	(C) Change in Spending on LTC/Elderly/Disabled in State After Applying State Savings, if Applicable (***)	(D) Change in Acute Care Spending on Non-Elderly After Applying State Savings if Applicable (****)	(E) Percentage Change in Total Medicaid Benefit Spending Taking All Effects Into Account
New England					
Connecticut	-158.3	191.8	-758.3	-158.3	-49.3%
Maine	-86.8	51.8	-180.3	-86.8	-38.9%
Massachusetts	-471.4	323.4	-419.8	-471.4	-25.0%
New Hampshire	-40.0	37.2	0.0	-34.7	-6.1%
Rhode Island	-30.4	73.8	-210.1	-30.4	-35.6%
Vermont	-31.3	18.4	-2.3	-31.3	-14.2%
Middle Atlantic					
New Jersey	-444.8	337.6	-18.1	-444.8	-12.8%
New York	-1,777.1	1,875.5	-5,784.7	-1,777.1	-44.3%
Pennsylvania	-689.4	392.1	864.9	-207.3	11.8%
South Atlantic					
Delaware	-31.5	22.9	-21.9	-31.5	-21.6%
District of Columbia	-87.5	57.5	-205.8	-87.5	-48.9%
Florida	-970.9	325.3	2,454.6	-645.6	38.4%
Georgia	-572.6	148.2	839.6	-426.4	16.6%
Maryland	-316.1	153.8	0.0	-356.6	-18.4%
North Carolina	-540.0	145.8	933.2	-394.2	21.1%
South Carolina	-267.5	81.8	354.4	-205.9	12.0%
Virginia	-223.0	150.1	360.0	-72.9	17.3%
West Virginia	-279.9	42.7	32.8	-237.2	-18.7%
East South Central					
Alabama	-236.5	82.8	823.8	-173.8	53.3%
Kentucky	-385.1	83.3	408.4	-301.8	6.2%
Mississippi	-249.9	37.9	485.3	-212.0	26.2%
Tennessee	-511.6	119.1	419.1	-392.5	1.2%
West South Central					
Arkansas	-174.4	50.5	303.9	-123.9	17.9%
Louisiana	-505.3	119.1	-128.1	-505.3	-23.2%
Oklahoma	-237.0	54.5	328.0	-182.5	13.6%
Texas	-1,454.2	292.6	1,769.2	-1,161.6	10.8%
East North Central					
Illinois	-707.8	410.2	63.9	-297.4	-4.9%
Indiana	-690.3	151.4	155.6	-547.9	-14.0%
Michigan	-680.1	283.1	-52.3	-680.1	-19.2%
Ohio	-831.9	320.1	0.0	-738.2	-15.6%
Wisconsin	-256.3	165.4	-137.5	-256.3	-18.7%
West North Central					
Iowa	-164.7	66.5	139.8	-98.2	4.2%
Kansas	-108.8	53.8	84.6	-55.2	4.2%
Minnesota	-284.3	180.5	-269.0	-284.3	-25.9%
Missouri	-222.6	116.1	393.2	-106.4	18.5%
Nebraska	-91.0	39.5	60.8	-51.5	1.7%
North Dakota	-41.7	14.6	-14.1	-41.7	-20.7%
South Dakota	-41.0	15.4	51.5	-25.6	9.7%
Mountain					
Arizona	n.a.	n.a.	n.a.	n.a.	n.a.
Colorado	-156.2	75.4	0.0	-103.4	-10.8%
Idaho	-56.2	15.0	72.1	-44.2	9.5%
Montana	-49.9	18.2	-25.4	-49.9	-23.3%
Nevada	-61.7	26.4	97.1	-35.3	18.0%
New Mexico	-144.8	23.7	83.6	-121.1	-6.7%
Utah	-161.1	15.7	15.3	-145.3	-27.5%
Wyoming	-32.9	7.0	6.3	-25.9	-14.8%
Pacific					
Alaska	-62.7	13.2	-27.3	-62.7	-38.3%
California	-2,232.1	799.0	857.7	-1,433.1	-5.2%
Hawaii	-56.4	27.6	114.5	-28.8	25.4%
Oregon	-189.5	58.6	224.9	-130.9	10.1%
Washington	-335.5	181.0	-383.8	-335.5	-34.9%

* High end price elasticity estimate (from Table 9) multiplied by current system acute care spending for the non-elderly (from Table 8, Total State less DSH less State Share of Administrative Costs)

** Low end of range estimate from Table 10

*** If Table 11, last column, shows a decrease in post-swap spending on long term care and acute care for the elderly and disabled in a state, then savings from column B Table 12 are applied to move these categories of spending back toward the status quo. If the last column of Table 11 shows a post-swap increase in spending, no savings from column B are applied here.

**** If there are state savings from column B in excess of those applied in column C, those savings are applied to increasing estimated spending on acute care for the non-elderly toward the level of the status quo.

***** Any state savings from column B in excess of those applied in column C or D are assumed to be used for other (non-Medicaid) public spending or for decreasing the state's private tax burden.

8/8/95 14:35

1. If the reallocation of dollars under the swap induced federalized long term care/elderly/disabled program results in a decrease in spending on these programs in a state, then we assume that state will use any newly available state funds to try to bring the swap long term care/elderly/disabled spending levels back to current system levels. Such newly available state funds come from the income effect resulting from the federalization. We assume that states will not increase long term care/elderly/disabled spending beyond current system levels.

If the reallocation of dollars under the swap induced federalized long term care/elderly/disabled program results in an increase in spending on these programs in a state, then we assume that the state will not use any newly available state funds for long term care/elderly/disabled spending.

2. If the state's income effect resulting from federalization exceeds the decrease (if any) in long term care/elderly/disabled spending in the state, then excess funds resulting from the income effect will be applied to the decrease in spending in the state on acute care for the non-elderly which resulted from the effective price increase on those services. We assume that states will not increase spending on acute care for the non-elderly to levels which exceed those in the current system.
3. If, after applying new state funds resulting from the income effect to long term care/elderly/disabled and non-elderly acute care, there are new funds remaining, then the excess of these funds is assumed to be spent on other public programs/services or be used to further decrease private sector tax burdens.

The assumption that increased state spending would first be used to bring state spending on long term care and acute spending for the elderly and disabled back up to current levels seems to be logical given the particular strength of long term care lobbies at the state level.

Column A of Tables 12 and 13 provide estimates of the decrease in state spending on acute care for the non-elderly due to the price effects detailed in Table 9. These estimates reflect the decreases before any new state funds are applied. Column B in each table shows the new funds available due to the income effect (previously seen in Table 10). Column C shows the change in long term care/elderly/disabled spending in a state after new state funds are applied to the new federal spending levels. Column D shows the change in acute care spending for the non-

elderly in the state following the application of excess state funds to these services. Column E contains estimates of the percentage change in total Medicaid spending, taking the income and price effects into account.

Under the optimistic scenario (Table 12), for the vast majority of states, the income effect from federalizing acute care for the elderly and disabled and long term care is sufficiently large that states would not see a decrease in spending on Medicaid services. There are four exceptions to this rule -- Connecticut, the District of Columbia, Maine, and New York would all experience decreases in acute care for the elderly and disabled/long term care and acute care for the non-elderly under this scenario. These four states all have large current system long term care/elderly and disabled acute programs relative to their share of low income elderly persons. Consequently, following federalization of these programs and reallocation of dollars according to the states' shares of low income elderly, these states suffer substantial decreases in their share of program spending. The income effect of federalization is not quite large enough to counteract these decreases. In terms of regional effects, the New England and East North Central states tend to experience total changes of relatively modest magnitudes, while the Southern states tend to see large relative gains in spending.

Under the pessimistic scenario (Table 13), all states would experience a decrease in at least one category of Medicaid spending -- acute care for the non-elderly/non-disabled. Large decreases seem to dominate the South Atlantic and East North Central states. Seventeen states would face a decline in long term care and elderly/disabled acute spending, with losers heavily concentrated in the New England region. Given some of the large increases in long term care and elderly/disabled acute spending in other states, total Medicaid spending on all programs would fall

for only 28 states, on net. The largest overall drops are for Connecticut (-49 percent), the District of Columbia (-49 percent), Maine (-39 percent), and New York (-44 percent), Rhode Island (-36 percent), Alaska (-38 percent), and Washington (-35 percent). States facing the largest benefit reductions are heavily concentrated in the New England and Pacific regions. Again, these are states with disproportionately large programs for long term care and acute elderly/disabled care under the current system.

The net increases for many states, however, disguise some significant drops in acute care spending for the non-elderly. This is particularly true in the East South Central and West South Central regions. Some notable examples of this phenomenon are Mississippi (a 66 percent drop in acute care spending), Kentucky (a 55 percent drop), Oklahoma (a 52 percent decline), and South Carolina (a 54 percent decrease). A similar scenario holds for some states which, on net, appear to have modest relative losses, but which suffer large percentage declines in acute care spending for the non-elderly. For example, North Dakota is estimated to have an overall spending decrease of approximately 21 percent, but its acute care decrease is estimated at 71 percent under this scenario. Montana, with an estimated net decrease of 23 percent, would experience a 69 percent drop in acute care spending under these assumptions. Consequently, when analyzing the impacts of a particular swap proposal, it is critical that attention not only be paid to aggregate spending effects, but that the effects on program components be studied as well.

V. Conclusions

One of the most appealing aspects of swap proposals is their presumed simplicity. In return for assuming some responsibilities at the federal level, states agree to take on other

programs. This should eliminate the complexity that arises when two different levels of government are involved in programs with shared responsibilities, such as AFDC and Medicaid. And, if the components are carefully chosen, presumably this could be a relatively budget neutral activity. Indeed, it is in this spirit that a number of swap proposals have been made, particularly those by Senator Nancy Kassebaum.

The economic theory of the division of responsibility between states and the federal government suggest a number of rationales. One test is whether a program exhibits a shared national purpose, such as defense, or whether there may be substantial economies of scale. Another is for programs where there are substantial spillover effects--that is, benefits to one state from activities that occur in another state. If these spillover effects are large, it makes sense for the national government to provide such services. When programs involve substantial redistribution of incomes, there is considerable sentiment that these should be done at a national level, although this has become a more controversial tenet in recent years. Differences around the country in preferences for services by states and localities may argue, on the other hand, for less-than-national provision.

In practice, however, the factors that lead to swap proposals are neither as theoretically justified nor as simple as we might otherwise expect. Indeed, many of the proposals divide up responsibility for relatively similar functions, justified more on the grounds of simplifying bureaucracy than on, for example, functional rationales for the appropriate levels of government. That is, various combinations of AFDC, food stamps, and Medicaid rearrangements involve programs which are all redistributive in nature. And, in practice, the goal of budget neutrality turns out to be a very complicated issue.

Even when assuming that levels of effort will remain perfectly constant, it is difficult to devise a program that is budget neutral at the federal level. The large programs commonly included in these proposals do not divide up evenly in aggregate. But even more importantly, proposals that are relatively budget neutral in aggregate nearly always result in substantial winners and losers across the various states. States not only vary enormously in the size of the various welfare programs under consideration, they also vary differentially depending upon particular parts of the programs. For example, some states are much more generous, relatively speaking, in terms of long term care services provided under Medicaid than they are in payment levels under AFDC, resulting in substantial variations in who gains and loses depending upon how a swap is structured.

But such an initial calculation is only part of the story. By design, a swap proposal will ultimately allow a state to vary the level and types of services it chooses to provide under a program that comes fully under its control. And the federal government, in turn, will undoubtedly seek to even out some of the differences across states in programs that it takes over. As should be apparent from the hypothetical example in this paper, estimating which states will ultimately win or lose after these behavioral adjustments take place is a very difficult task.

The simple view of a swap is often that a state will simply take the funds freed up from the federalized programs and apply them to the program now under their control and hence spending will remain about the same. But economic theory suggests that the process is likely to be much more complicated. First, dollars freed up in the state when the federal government takes over an activity are not likely to all be devoted to the “swapped” program now fully under the state’s control. Indeed, not all of those funds will even remain in the public sector. Theory also suggests

that when a state takes over a program that was previously subsidized by the federal government, spending will tend to fall because the “price” of providing each service has effectively increased. It is the combination of the new resources available to spend and the higher price of the swapped program that will determine what happens at the state level.

Our results in the example presented suggest substantial potential changes in spending beyond what a simple maintenance of effort approach would predict, but we are also well aware of the difficulties of specifying and then estimating the likely effects. Swap proposals in practice are likely to bring about some surprising results that go well beyond what simple estimates of initial winners and losers suggest.

Appendix-A

The Components of the Price Effect

The price effect is composed of two distinct phenomenon: a substitution effect and an income effect. The substitution effect occurs because the current effective price (CEP) of the devolved Medicaid services facing each state increases from:

$$CEP = (1 - FMAP) * P_M,$$

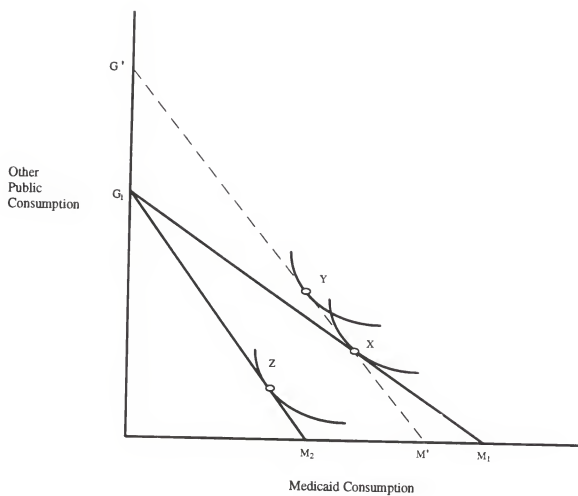
a value less than P_M , to a new effective price (NEP) of:

$$NEP = P_M$$

where FMAP is the current federal matching assistance percentage and P_M is the actual market price of services for the Medicaid program. As the price of services increases, theory tells us that the demand for those services will decline, as long as the state government perceives Medicaid services to be a normal good. The income effect component of the price effect occurs because the change in price of Medicaid services effectively reduces states' purchasing power. These two component effects are illustrated in Figure A.

Line segment G_1 - M_1 represents a state's budget constraint under current law (taking the federal matching rate into account). A state can purchase M_1 Medicaid services, or G_1 other government goods and services, or any combination of the two that falls on that line segment. This state's preferred combination of Medicaid and other services is shown by point X. If price is

FIGURE A



changed but purchasing power is held constant, the budget constraint rotates around point X as shown by the dotted line segment $G'M'$. The implication of this line is that state government income is increased just enough to make the original choice set still affordable. As the price of the normal good (Medicaid) increases, however, the state is likely to choose to purchase less of it, a movement illustrated by choice set Y. This movement in the choice set (from X to Y) is referred to as the substitution effect. The slope of this dotted line is determined by the new effective price of Medicaid services relative to all other goods and services.

If total government income were to remain unchanged, however, and prices were changed as noted above, the budget constraint would shift in a parallel fashion from $G'M'$ to G_1M_2 . The preferences of this state would result in a choice set of Medicaid and other governments goods and services represented by point Z. The movement from point Y to point Z is referred to as the income effect. The combination of the substitution and income effects, the move from choice set X to choice set Z, is what is observed as a consequence of a change in effective price, that is, the elimination of the federal matching contribution for a portion of the Medicaid program

Appendix-B

Calculation of High End Elasticities

Gramlich's (1982) preferred equation for estimating the natural log of AFDC benefits is as follows:

$$\ln B = \beta_1 \ln Y + \beta_2 \ln s + \beta_3 \ln A + \ln F$$

where B is the state AFDC benefit level, Y is the state average per capita income, s is the state's share of AFDC benefits, A is the average AFDC benefit level across all other states, and F is the food stamp benefits. Gramlich's estimate of β_2 is .957. We assume that this relationship between the state share and the benefit level has persisted over time, and that the price response is also applicable to the Medicaid program.

We set K equal to:

$$K = \beta_1 \ln Y + \beta_3 \ln A + \ln F$$

so that,

$$\ln B = K + \beta_2 \ln s$$

We simulate K using 1993 data as:

$$K = \ln M_{1993} - \ln s_{1993}(-.957)$$

where M_{1993} is the total Medicaid spending in the state in 1993 and s_{1993} is the state share of Medicaid spending in 1993. Estimated values of K are shown in column B of the appendix table.

We can then calculate the percentage change in Medicaid spending in each state if the state match had been increased from its actual 1993 level to 100%, as would be the case under a swap. The benefit level under the swap (100% state share) would be equal to:

$$\ln M_{\text{swap}} = K + \ln(1) * -.957 = K$$

with M_{swap} equal to e^K . The percentage change in spending following the swap would therefore be:

$$\% \text{ change} = \frac{M_{1993} - M_{\text{swap}}}{M_{1993}} = \frac{M_{1993} - e^K}{M_{1993}}$$

where ‘% change’ is the percentage change in Medicaid spending given an increase in the state share from the 1993 level to 100 percent. The estimated percentage change in spending for each state is shown column C of the appendix table. In order to calculate an implied elasticity for each state that would be comparable to Orr’s estimate of -.23, we would divide ‘% change’ by the percentage increase in price for each state. The implied elasticity for each state is shown in column E of the table.

Appendix Table
Calculation of Price Elasticities Implied by Gramlich (1992)

State	(A) Medicaid Benefits for Aged Care of the Non-Elderly/Non-Disabled FY 1993 ('B 1993')	(B) Estimated Value of "K" (*)	(C) Estimated % Change in Spending Given Relative Price Increase from 1993 State Share to 100% (**)	(D) % Change in Relative Price from 1993 State Share to 100% (***)	(E) Implied Price Elasticity (****)
New England					
Connecticut	326.4	5.3620	-48.5%	66.7%	-72.7%
Maine	144.2	3.8950	-60.2%	89.5%	-67.3%
Massachusetts	972.2	6.0465	-48.5%	66.7%	-72.7%
New Hampshire	82.5	3.4750	-48.5%	66.7%	-72.7%
Rhode Island	96.8	4.2088	-52.1%	73.3%	-71.1%
Vermont	53.7	3.3844	-58.3%	85.5%	-68.2%
Middle Atlantic					
New Jersey	917.4	5.8648	-48.5%	66.7%	-72.7%
New York	3,665.2	7.4121	-48.5%	66.7%	-72.7%
Pennsylvania	1,279.0	8.1369	-53.9%	76.8%	-70.2%
South Atlantic					
Delaware	65.0	3.1675	-48.5%	66.7%	-72.7%
District of Columbia	180.5	4.2819	-48.5%	66.7%	-72.7%
Florida	1,816.2	8.0709	-53.5%	75.9%	-70.4%
Georgia	947.1	5.2640	-60.5%	90.0%	-67.2%
Maryland	852.0	5.2084	-48.5%	66.7%	-72.7%
North Carolina	839.7	4.9857	-54.3%	98.3%	-65.4%
South Carolina	383.8	3.7253	-69.7%	110.8%	-62.9%
Virginia	460.0	4.9567	-48.5%	66.7%	-72.7%
West Virginia	374.4	3.4793	-74.8%	123.3%	-60.6%
East South Central					
Alabama	338.5	3.5548	-69.9%	111.2%	-62.9%
Kentucky	549.3	4.3098	-70.1%	111.7%	-62.7%
Mississippi	322.2	3.1132	-77.6%	130.6%	-59.4%
Tennessee	775.7	4.4722	-66.0%	102.0%	-64.6%
West South Central					
Arkansas	239.3	2.9820	-72.9%	118.5%	-61.5%
Louisiana	700.3	4.0067	-72.2%	116.7%	-63.7%
Oklahoma	348.1	4.2092	-68.1%	106.9%	-63.7%
Texas	2,314.7	5.4276	-62.8%	95.1%	-66.1%
East North Central					
Illinois	1,459.4	6.2036	-48.5%	66.7%	-72.7%
Indiana	1,135.3	4.6258	-61.6%	92.4%	-66.6%
Michigan	1,253.4	6.4321	-54.3%	77.5%	-70.0%
Ohio	1,418.7	6.1063	-56.6%	66.2%	-68.0%
Wisconsin	435.8	5.3023	-48.5%	66.5%	-67.9%
West North Central					
Iowa	269.5	4.2537	-61.1%	91.4%	-66.9%
Kansas	192.3	4.1643	-56.6%	82.0%	-69.0%
Minnesota	532.7	5.3275	-53.4%	75.7%	-70.5%
Missouri	379.5	4.8783	-58.7%	86.2%	-68.0%
Nebraska	152.5	3.4426	-59.7%	88.4%	-67.5%
North Dakota	59.1	2.2340	-70.6%	113.0%	-62.5%
South Dakota	59.7	2.1926	-68.7%	108.3%	-63.4%
Mountain					
Arizona	n/a	n/a	n/a	n/a	n/a
Colorado	299.4	4.4888	-52.9%	74.8%	-70.7%
Idaho	85.0	2.4142	-69.6%	110.6%	-63.0%
Montana	71.9	2.8919	-69.3%	109.9%	-63.1%
Nevada	121.7	3.2865	-50.7%	70.8%	-71.7%
New Mexico	200.3	3.5847	-72.3%	117.1%	-61.1%
Utah	218.4	3.2054	-73.8%	120.7%	-61.1%
Wyoming	50.2	2.3437	-65.5%	101.0%	-64.9%
Pacific					
Alaska	129.4	4.1200	-48.5%	66.7%	-72.7%
California	4,603.5	8.0983	-48.5%	66.7%	-72.7%
Hawaii	116.3	4.3651	-48.5%	66.7%	-72.7%
Oregon	311.7	4.5473	-60.8%	90.7%	-67.0%
Washington	627.7	5.7470	-53.4%	75.9%	-70.4%

* See appendix text for detailed explanation. K is equal to the natural log of column A minus the natural log of the state's 1993 Medicaid share multiplied by the estimated coefficient on state share (i.e. 957).

** See appendix text for detailed explanation. % change is equal to column A minus EXP(K), divided by column A.

*** Percentage change in price is equal to (1-state share)/(average of 1 and state share).

**** Implied elasticity is equal to column C divided by column D.

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